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IN THE

# SUPREME COURT

OF THE
UNITED STATES
OCTOBER TERM, 1979

No. 78-1201

MOBIL OIL CORPORATION,

*Appellant,*

—VS.—

COMMISSIONER OF TAXES OF VERMONT,

*Appellee.*

On Appeal From the Supreme Court of Vermont

## BRIEF OF MULTISTATE TAX COMMISSION AND PARTICIPATING STATES AS AMICUS CURIAE ON BEHALF OF APPELLEE

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### INTRODUCTORY STATEMENT

This brief is submitted by the Multistate Tax Commission and the states which have joined in this brief as amicus curiae in support of the appellee. Both parties to this proceeding have consented to the filing of this brief.[1]

---

[1]Originals of the letter received from the parties, evidencing this consent, have been filed with the Clerk of the Court.

## STATEMENT OF INTEREST

The Multistate Tax Commission (hereinafter referred to as the "MTC") is the administrative agency of the Multistate Tax Compact entered into currently by 19 states as full members and by 12 states as associate members.[2]

The purposes of the Compact are to:

1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.

2. Promote uniformity or compatibility in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and other phases of tax administration.

4. Avoid duplicate taxation.[3]

The MTC seeks uniformity in state tax treatment of multistate-multinational businesses, and fairness and equity between such businesses and smaller in-state businesses. It is also working to advance effective enforcement of state corporate tax laws, and seeks policies which are simple and comprehensible for public officials and business taxpayers alike.

In fulfillment of these objectives in the area of state income taxation of multistate-multinational businesses,

[2]The current regular members are the states of Alasks, Arkansas, California, Colorado, Hawaii, Idaho, Kansas, Michigan, Missouri, Montana, Nebraska, New Mexico, Nevada, North Dakota, Oregon, South Dakota, Texas, Utah and Washington. The associate members are the states of Alabama, Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Pennsylvania, Tennessee, and West Virginia. (Ninth Annual Report, Multistate Tax Commission, June 30, 1976.)

[3]The constitutionality of the Compact was upheld in *U.S. Steel, et al. v. Multistate Tax Commission, et al.*, 434 U.S. 452 (1978), affirming 417 F. Supp. 795 (S.D.N.Y. 1976). This Court there noted that the Compact "* * * symbolized the recognition that, as applied to multistate businesses, traditional state tax administration was inefficient and costly to both State and taxpayer."



Article IV of the Compact sets forth the provisions of the Uniform Division of Income For Tax Purposes Act (UDITPA).[4]

It is important that this language be interpreted to carry out the purpose of the 29 states in adopting UDITPA. This purpose is to provide for uniformity and full accountability (without duplication) in the division of income for state income tax purposes by workable and rational division of income rules.

Pursuant to its authority under Article VII of the Compact, on February 21, 1973, the Commission approved revised uniform allocation and apportionment regulations which implement UDITPA. It is estimated that 18 states have adopted these regulations substantially in the form as adopted by the Commission.[5]

The present case raises matters of vital interest to the MTC and the states. They are concerned with the proposition advanced by Mobil, C.O.S.T. and the N.A.M. that, under the Constitution of the United States, dividends (and presumably other income from intangible

[4]UDITPA was promulgated by the National Conference of Commissioners on Uniform State Laws in 1957 (Uniform Laws Annotated, Vol. 9a, p. 448 et seq). It has been adopted by a great majority of the income tax states (Eleventh Annual Report of the Multistate Tax Commission (1977-1978), Appendix B, p. 28). Its purpose is to provide for the uniform allocation and apportionment of income for state income tax purposes by those states that adopt it. Section 1(a) defines "business income" which is subject to apportionment as:

> "* * * income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

Section (e) defines "nonbusiness income" which is subject to specific allocation as:

> "* * * all income other than business income."

[5]Results of a Survey on the Uniformity of State Laws by the State of Indiana dated February 15, 1977.

properties based on the nature of their arguments)[6] must be arbitrarily assigned to the "commercial domicile" of the payee corporation rather than to where the taxpayer utilizes these intangible properties and the income derived therefrom in conducting its unitary activities, as required by a reasonable interpretation and application of the Vermont corporate income tax law.

More specifically, they are concerned with an interpretation of the commerce clause which would prevent, in practical operation and effect, any significant state income taxation of large, complex, integrated domestic multinational corporations. If Mobil's position is sustained by this Court, they believe that these corporations, which conduct their unitary business operations throughout the world through numerous affiliated and subsidiary corporations, can escape from any significant state income taxes by obtaining their profits from these business operations in the form of income from intangibles from their subsidiary and affiliated corporations and by attributing such income to states where it is not taxed by application of the illusive legal fiction "commercial domicile."[7]

[6]Although Mobil limits its appeal to so-called "foreign source" dividends, it and its amicus curiae do not contend that their constitutional arguments can be so limited. Mobil's constitutional arguments and that of its amicus would appear to apply with equal validity (or invalidity) to any other form of income from intangibles such as income from royalties, patents, trademarks, goodwill, contractual obligations, interest, etc. In fact, their arguments could apply to any "property" which they could label as producing "foreign source" income.

[7]In regard to the "commercial domicile," no significant income producing activity takes place at the commercial domicile as pertains to passive "investments" in wholly owned and created subsidiary corporations which justifies the taxation of the great bulk of the income of multinational corporations by the state of "commercial domicile." For example, we believe that an indepth analysis of Mobil's activities would reveal that its so-called "dividend" income is attributable to its involvement in and management of a worldwide petroleum and petroleum related business rather than to "investments" as such in the stocks of its subsidiary and affiliated corporations.



The Commission and the participating states are especially concerned in preventing any resolution of this case from spilling over indiscriminately into their state tax policies represented by the carefully thought-out and reasonable attribution rules incorporated in the language of UDITPA[8] and comparable income tax attribution laws.

We are also concerned that vaguely defined foreign tax policies, which allegedly shape federal income tax consequences, may be utilized as a constitutional standard to prevent a fair and uniform state or local tax system which is necessarily dependent upon different policies and jurisdictional prerequisites. In this connection we are particularly disturbed by the position of Mobil and its amicus curiae that alleged international tax policy of the United States *designed solely to protect the United States citizens, residents and corporations from discriminatory or inappropriate taxation by other nations* dictates how the states and their political subdivisions may constitutionally tax domestic United States corporations. We are particularly concerned on reliance of such an argument to invalidate a state income tax law which is confined solely to a reasonable apportionment of "federal taxable income" attributable to that part of a unitary business conducted in the taxing state.

[8]If this Court should hold, as a matter of constitutional law, apart from factual underpinnings, that dividends from "foreign sources" are subject to tax only at the commercial domicile, it would cast a serious cloud on the constitutionality of the apportionment rules of UDITPA pertaining to all forms of income from intangible properties. While UDITPA, unlike the Vermont income tax law, specifically requires the apportionment of dividends and other income from intangibles only if such income is connected with the unitary business of the taxpayer which is carried on in part in the taxing state and requires the specific allocation of this income if not so connected, we discern nothing in the general abstract constitutional arguments of Mobil and its amicus which would distinguish UDITPA from the Vermont law. They are not here contending that the Vermont law, which apportions "federal taxable income" by a three-factor apportionment formula, in fact is intended to or in fact includes in apportionable income any income of Mobil which is not connected with Mobil's unitary business conducted in part in Vermont for the years in question.

Of concern also is the position of Mobil and its amicus curiae that this Court should resort to hypothetical constitutional reasoning and legal fictions to prevent what they label as a "risk of multiple taxation" because of the lack of uniformity in state income attribution rules. As a matter of fact, this lack of uniformity has never been shown to result in any duplicate taxation of the income of any multinational corporations such as Mobil and the members of C.O.S.T. and the N.A.M. In fact, based upon such argument, Mobil here contends that virtually all of its net income should be exempt from any state taxation whatsoever. As a practical matter, Mobil's and its amicus' constitutional equation is that "risk of multiple taxation equals tax preference or immunity."[9]

Finally, the states have a vital interest in assuring that all businesses carrying on activities within their jurisdictions, and benefiting from governmental services and functions, bear their fair share of the public cost of these activities. This is not just a question of revenues, it is a question of tax justice as well.[10]

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[9]In this connection, we are confident that if the present state tax system in fact resulted in any duplicate taxation of the total income of any multinational corporation participating in this litigation, such as C.O.S.T. or N.A.M. members, any such dramatic and significant results would have been brought to the attention of this Court. To our knowledge, no such result has ever been presented to a state tax administrator. Furthermore, if it were, we have been assured by many state tax administrators that such a result would trigger a basis for administrative relief. In fact, based on the experience of the MTC, the failure to achieve better uniformity in state income tax attribution rules and the resistance of C.O.S.T. and the N.A.M. to the Multistate Tax Compact (which makes available the UDITPA attribution rules *as an option* to the taxpayer) stems from the fact that the present attribution rules result in substantial undertaxation of the income of large influential multinational corporations such as the members of C.O.S.T.

[10]It is imperative that state and local taxes bear as even-handedly as possible on all business activities conducted within the respective state and local jurisdictions. Only in this manner can small interstate businesses, which are still the foundation of our free enterprize system, hope to compete with their larger multistate-multinational competitors. Only in this manner can these competitors also receive tax equity and



In regard to corporate privilege taxes on or measured by net income, we believe that this can be best accomplished by reasonable apportionment of the income of a unitary trade or business carried on in part in the taxing state rather than by resorting to the illusive legal fiction of "commercial domicile" which is subject to manipulation and control solely in the discretion and judgment of multinational corporations.[11]

In addition to the foregoing, as a pragmatic proposition, we are concerned with the status of the record in this cause in light of the broad factual and legal conclusions which Mobil and its amicus rely on in support of their constitutional arguments.[12]

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fairness. In the instant case, however, Mobil and its amicus would require Vermont to tax Mobil's instate competitors on an entirely different basis than it taxes Mobil, with the result that Mobil is virtually free for the years in question from any state income taxes except for those states which utilize combined reporting. If constitutionally possible, any such result should be avoided.

[11]Tax jurisdiction based upon "commercial domicile" in the light of modern business practices of multinational corporations may involve no more tax substance as pertains to intangible properties and income therefrom than the traditional reliance on the state of incorporation ("legal" domicile.)

The general nature of the problems involved are discussed in Dexter, "Taxation of Income from Intangibles of Multistate-Multinational Corporations," 29 Vand. L. Rev. 401 (1976) and Corrigan, "Interstate Corporate Income Taxation—Recent Revolutions and a Modern Response," *Ibid.*, p. 423.

[12]As we view Mobil's due process and commerce clause arguments, they are founded on the totally unsupported proposition that its so-called "investments" in wholly owned subsidiary corporations (which it undoubtedly created to carry on its integrated, interrelated "unitary" worldwide petroleum and petroleum-related business) is completely unrelated to those aspects of this business which it carried on for the years in question in Vermont. However, there is absolutely nothing in the record in this cause to substantiate this argument except that it manages its "investments" and income therefrom from without Vermont. Nor is there any factual support for Mobil's "multiple risk" commerce clause argument. Mobil assumes that existing differences in state allocation and apportionment rules produces multiple taxation when in fact, as applied to Mobil, the exact opposite is true. Inasmuch as Mobil has the burden of proof to establish the unconstitutionality of the Vermont corporate income tax law as applied to it, the factual gaps in the record must be resolved in favor of Vermont.

## COUNTERSTATEMENT OF QUESTIONS INVOLVED

We cannot accept Mobil's statement of questions involved.[13]

We believe the issue in this case may be properly framed as follows:

Is a state corporate privilege tax, on or measured by that portion of a corporation's federal taxable income which is attributable to the state by the generally accepted and used three-factor apportionment formula, invalid under either the due process clause or commerce clause of the Constitution of the United States (A) when applied to a taxpayer that failed to prove either (1) that income attributable to the taxing state is not a reasonable measure of its corporate privileges, income and benefits associated with activities in the taxing state; or (2) that the income subject to apportionment is not derived by the taxpayer from properties which are utilized by the taxpayer in the

[13]Question 1 as presented by Mobil is predicated on several false premises, including (1) that inclusion of gross dividend income in an apportionable tax base constitutes the taxation of such gross dividends; and (2) that Mobil's gross dividends (primarily derived from four subsidiary and affiliated corporations) is completely disassociated from its unitary business which it carried on in part in Vermont. We believe the facts that (1) Vermont is not attempting to tax Mobil's dividend income by application of its apportionment formula to Mobil's federal taxable income, any more than it is attempting to tax Mobil's income from out-of-state refining and other operations; and (2) Mobil's presumed utilization of its dividend income and stocks in connection with its unitary business carried on in part in Vermont, alone disposes of Mobil's due process of law argument.

In regard to Mobil's second question presented, irrespective of how Mobil would construe foreign commerce clause limitations on state taxing power, there is absolutely nothing in the record to support its argument that the inclusion of so-called "foreign source dividends" in an apportionable income tax base constitutes a taxation of income from or activities in foreign commerce or subjects these dividends to any greater risk of multiple taxation that would the taxation of such dividends by the commercial domicile.

The third question presented by Mobil, its argument that the taxation of foreign source dividends on an apportionment basis conflicts with established federal policy in regulating foreign commerce, totally lacks any legal or factual foundation.



conduct of a unitary business which it conducts both within and without the taxing state; and (B) when dividends from the taxpayer's stock in its foreign subsidiary and affiliated corporations is included in federal taxable income even though the taxpayer's activities in regard thereto takes place without the taxing state and the taxpayer maintains its legal and commercial domicile without the taxing state.

## STATEMENT OF THE CASE

### A. HISTORY OF PROCEEDINGS.

§ 5831 of Vermont Law[14] imposes the Vermont corporate income tax on the income earned or received in the taxable year by every corporation at a 6% flat rate for the years in question. § 5811(18) defines the tax base subject to apportionment as "the taxable income of the taxpayer for that taxable year under the laws of the United States, excluding income which under the laws of the United States is exempt from taxation by the states." § 5833 provides for the apportionment of a corporation's income by the generally accepted and used three-factor apportionment formula if its income is "derived from any trade, business or activity conducted both within and without" Vermont.[15]

§ 5833 further provides in subsection (b) that if the apportionment formula as applied to a corporation's trade, business or activity conducted both within and without Vermont, does not fairly represent the extent of the business activities of the corporation within Vermont:

> "* * * the corporation may petition for, or the Commissioner may require, with respect to all or any part of the corporation's business activity, if reasonable: (1) separate accounting; (2) the exclusion or modification of any or all of the factors; (3) the

[14]References herein are to sections of 32 Vermont Statutes Annotated (V.S.A.)

[15]This statutory framework is explained in greater detail in the opinion of the Vermont Supreme Court at pages 19a-20a of the Jurisdictional Statement.

inclusion of one or more additional factors which will fairly represent the corporation's business activity in this state; or (4) the employment of any other method to effectuate an equitable allocation and apportionment of the corporation's income."

Without requesting any relief permitted by § 5833(b), Mobil filed its Vermont corporate income tax returns[16] for tax years 1970, 1971 and 1972 (the years in question) by deducting from its federal taxable income all of its gross dividend and an unexplained portion of its gross interest income, as well as "foreign taxes" which were not deductible in arriving at "federal taxable income."

For the year 1970, the dividend exemption taken by Mobil on its Vermont corporate income tax return amounted to $174,211,073.60 of the total federal taxable income of $220,035,244.23 or *79%* of its federal taxable income (A37); for the year 1971, $282,217,008.65 of federal taxable income of $308,255,570.02 or *92%* (A51); and for the tax year 1972, *121%* (A65). In arriving at federal taxable income, Mobil deducted all of its expenses, *including interest and all general offices and overhead expenses* and other deductions such as depletion, intangible drilling costs, etc., presumably as allowed for federal income tax purposes. The factors in the apportionment formula indicate, as shown on Mobil's returns, that all of its property, payroll and sales were included in the denominators (*including any overhead, payroll and property utilized in its so-called "investment" activities* and any sales or service receipts from its subsidiary and affiliated corporations).

[16]While the record does not disclose on what basis Mobil filed its federal income tax returns, the schedules from these returns (A38-A45, A52-A59, A66-A73) indicates that Mobil filed its federal income tax returns for the years in question on a consolidated reporting basis. Thus "federal taxable income" on Mobil's Vermont returns are *pro forma* returns which are products of Mobil's "separate accounting" in regard to any transactions or dealings with its subsidiary and affiliated corporations. What constitutes its dividends from its subsidiary and affiliated corporations is a product of this "separate accounting."



Mobil thus deducted from its Vermont tax base subject to apportionment all of its costs relative to its activities pertaining to its "investments" and included in its out-of-state tangible property, payroll and sales all of its tangible property, payroll and sales pertaining to its "investments."

These returns further indicate that it had property, payroll and sales in Vermont as follows:

| YEAR | PROPERTY* | PAYROLL | SALES |
|---|---|---|---|
| 1970 | $3,930,100(A36) | $236,553(A35) | $8,554,200(A35) |
| 1971 | $6,707,534(A50) | $244,577(A49) | $9,175,931(A49) |
| 1972 | $8,236,792(A64) | $254,938(A63) | $9,589,447(A63) |

*Includes capitalized rental properties.

As a result of averaging the foregoing Vermont numerators to the everywhere denominators of Mobil, the Vermont apportionment factor apportioned .146032% of Mobil's taxable base income to Vermont for 1970, .173647% for 1971 and .182151% for 1972 (A36, A50 and A64 respectively).

These factors, after the deduction of the dividends includable in federal taxable income, would attribute $63,772 of income to Vermont for the tax year 1970, $45,038 for 1971 and a minus $87,064 for 1972 for a *net total of $21,496*. Yet, as indicated by the apportionment factors disclosed on Mobil's returns for the years 1970-72, Mobil increased its investment in tangible properties in Vermont from $3,508,596 at the beginning of 1969 to $6,328,183 at the end of 1972 or a total increase of $2,819,587.

From the property everywhere factor (denominator of the factor), as disclosed on Mobil's returns, the tangible property values of Mobil increased from $2,388,272,971 beginning in 1970 to $2,864,792,471 at the end of 1972, or by approximately one-half billion dollars. This amount is in excess of Mobil's federal taxable income minus its dividends included therein ($24,322,057, which constitutes the income it would attribute to its business activities conducted in part in Vermont) by $452,196,443 for the years in question.

From an examination of Mobil's balance sheets for the years 1970-1972, filed with its Vermont and federal income tax returns for these years (A44; A58; A72), there is no indication that its total income for these years was not utilized by Mobil in furtherance of its overall business activities which it has attributed, in part, to Vermont for the years in question.[17]

An examination of the *pro forma* U.S. Corporate Income Tax Returns of Mobil, Form 1120, page 1, accompanying its Vermont tax returns for the years 1970-1972 (A38-39; A52-53; A66-67) also denotes the integrated nature of Mobil's business activities. The only adjustments that Mobil made to its federal taxable income for Vermont income tax purposes for the years in question consisted simply of arbitrarily deducting as "non-apportionable income" its gross dividend income to the extent included in federal taxable income, an undisclosed and unexplained portion of its gross interest income and "foreign taxes not deductable for federal income tax purposes." (A37, A51, A65)

After these adjustments to federal taxable income, Mobil simply applied the Vermont apportionment formula, determined by reference to Mobil's total tangible properties, payrolls and sales (irrespective of location, nature source or use) to its Vermont tangible property, payroll and sales. In other words, Mobil filed its Vermont income tax returns on the basis that all of its business activities and expenses and income derived therefrom, were directly related to the conduct of a unitary business both within and without Vermont. Inconsistent therewith, without explanation, it deducted the dividend income here

[17]During this period, its total assets increased by approximately 1.1875 billion dollars and its liabilities increased by approximately 401.8 million dollars. During this period its cash decreased by 92 million dollars, its trade accounts increased by 29.3 million dollars, its other current assets by approximately 75.9 million dollars, its buildings and fixed assets increased by 518.9 million dollars, land net of amortization increased by 102.8 million dollars and other investments increased by 3.826 billion dollars.



in question, as well as interest and foreign taxes, from federal taxable income for Vermont apportionment purposes.

Based on the returns as filed, Mobil paid a Vermont tax of $1,821 for 1970, and a minimum tax of $25.00 for the years of 1971 and 1972 (A34, A48, A62), which tax equals *.00000684%* of its Vermont sales for these years.

Apparently, as a result of a desk audit of Mobil's 1970-1972 returns, Vermont concluded that Mobil had not shown any justification under the Vermont statutes or laws of the United States why its dividend income, interest income and "foreign taxes" (which were not deductable for federal income tax purposes) should be deducted from Mobil's income subject to apportionment. Vermont thus determined that Mobil's corporate income tax liability should be in the amount of $71,643.77 for the years 1970-1972 (Juris. St. App. A, 1a). This represents a tax of *.00026229%* of Mobil's Vermont sales for these years.

Mobil objected to this result and requested and obtained an administrative hearing before the Commissioner of Taxes of Vermont in regard thereto. At the hearing, counsel for Mobil proferred a Stipulation of Facts, which was accepted as the "testimony" of Mobil's counsel (A17).[18]

[18]This "Stipulation of Facts" is set forth on pages A79-A91 of the appendix, except for the exhibits, other than Exhibits 1, 2, 3 and 8, referred to therein and made a part of the record. Exhibits 1, 2 and 3 are the Vermont corporate income tax returns for each calendar year 1970, 1971 and 1972 of Mobil (A37-A73); Exhibits 4, 5 and 6 are the assessments in question; Exhibit 7 is Mobil's protest to the assessments; Exhibit 8 is the schedule of Mobil's dividend income by amount and payor corporation for the years 1971-1972 (A75-78); and Exhibits 9, 10, 11, 12, 13 and 14 are Mobil's annual reports and financial and operating statistics for the years 1970, 1971 and 1972. Exhibit 15 lists affiliated companies included in such reports.

Paragraphs (6) through (35), together with Exhibits 8-15 of the "Stipulation," contain the factual material submitted by Mobil in support of its position.

Based on this factual information, Mobil argued before the Commissioner that inclusion of its dividend income in apportionable income amounted to taxation of the dividends, in violation of due process of law limitations, because, "* * * there is simply no relationship between this income which is sought to be taxed and the state of Vermont." (A20) Based on this conclusion and the further conclusions that: (1) the commercial domicile had the power to tax the dividend and interest income in full; and, (2) the commerce clause prevents any risk of multiple taxation, Mobil further argued that the inclusion of dividend income in apportionable income was invalid under the commerce clause.

As part of its commerce clause argument, Mobil further argued that the inclusion of dividend income in Vermont apportionable income constituted the taxation of foreign commerce, in controvention of the power of Congress to regulate commerce with foreign countries.

The only facts in the record in support of Mobil's argument here are those contained in paragraphs 6-12, 25, 26 and 33 of the "Stipulation."[19]

[19]These paragraphs read:

(6) Mobil is engaged in the petroleum business in the United States, including exploration, production, refining, transportation, distribution and sale of petroleum and petroleum products. In addition Mobil conducts petro-chemical, chemical coatings, plastics and phosphate rock mining businesses in the United States.

(7) Mobil's corporate headquarters, principal place of business and commercial domicile are not in Vermont but are located at 150 East 42nd Street, New York, New York. *Mobil's business is not managed, controlled or directed from the State of Vermont.*

(8) *Mobile does business in all of the states* of the United States, the District of Columbia, has a small branch in Greece and engages in interstate and foreign commerce. Mobil is *subject to net income taxes or franchise taxes measured by net income imposed by some forty other states* and the District of Columbia.

(9) Mobil's only activity within the State of Vermont is the wholesale and retail marketing of petroleum products and related products. Mobil has no refineries or oil or gas production within the State of Vermont.



In regard to the stipulation of facts, it is of critical importance in this case to note that Mobil did not establish or seek to establish that the stock investments in question and the dividends derived therefrom were assets which were unrelated to its unitary business, which it carried on in part in Vermont and which business was the subject matter of the Vermont apportionment formula. Mobil sought only to establish that its activities in regard to these assets were not conducted in Vermont. Furthermore, Mobil offered no proof and did not contend that any

(10) Mobil owns directly and indirectly capital stock of a large number of foreign subsidiary and domestic and foreign nonsubsidiary corporations. At December 31st of each year Mobil owned directly or indirectly capital stock of foreign subsidiary and 5% or more of domestic and foreign nonsubsidiary corporations as follows:

| | 1970 | 1971 | 1972 |
|---|---|---|---|
| Foreign Subsidiary Corporations | 203 | 208 | 216 |
| Domestic Nonsubsidiary Corporations | 26 | 27 | 27 |
| Foreign Nonsubsidiary Corporations | 185 | 189 | 197 |

(11) *The aforementioned capital stocks were held, managed and controlled by Mobil from its offices outside Vermont. Payment of all dividends was received by Mobil outside Vermont and Mobil's control, use and disposition of such dividends were managed and directed from Mobil's offices outside Vermont.*

(12) There is attached as Exhibit 8 a schedule of Mobil's dividend income for the years 1970 through 1972 subjected to tax by the assessments of the Department of Taxes of the State of Vermont.

(25) None of the corporations listed in Exhibit 8 which are 5% or more owned by Mobil is organized under the laws of Vermont, did business in Vermont, owned or leased property in Vermont, maintained an office in Vermont, had employees in Vermont or derived income from sources in Vermont. With respect to the corporations listed in Exhibit 8 as to which Mobil owns less than 5%, to the best of Mobil's knowledge and information the foregoing statements likewise apply.

(26) More than 99% of the dividends here in issue were received from corporations deriving all or all but an insignificant portion of their income from sources outside the United States.

* * * * *

(33) The income of each of the corporations referred to in paragraphs 26 to 32 inclusive were derived to a substantial extent from foreign commerce. (Emphasis added.)

of its dividend income was in fact taxed by any state or country on the basis of specific allocation of this income or that it paid any taxes to other countries.

Based on the foregoing record and argument and *Woolworth v. Commissioner of Taxes*, 130 Vt. 544, 298 A.2d 839 (1972), [including the Supreme Court of Vermont's reliance therein on *Woolworth Co. v. Director, Division of Taxation*, 45 N.J. 466, 213 A.2d 1 (1965) and other unitary cases], the Commissioner of Taxes applied the unitary concept in upholding the assessments against Mobil for the years 1970-1972.[20] (Juris. St. App. A, pp. 1a-13a). Mobil's arguments before the Vermont courts were limited to its "multiple risk" commerce clause argument.[21]

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[20]Significantly, the Commissioner of Taxes stated:

The Vermont Supreme Court in the *Woolworth* decision specifically stated at 130 Vt. 544, 549:

> In its holding the court in *Gulf Oil Corp. v. Morrison*, supra, 120 Vt. 330 held the inclusion of dividends in the allocation formula did not serve to make the formula operate in an arbitrary manner.
>
> * * *
>
> This court's approach towards the inclusion of such items of net income as dividends and capital gains in the allocation formula for franchise taxation purposes has been accepted in other jurisdictions. The basic rationale of their inclusion was state in *F. W. Woolworth Co. v. Director, Division of Taxation*, 45 N.J. 466, 213 A.2d 1, 9 (1965) where that court said:
>
> * * *
>
> the realistic value of the exercise of a franchise in a particular state is enhanced and contributed to by the worth or income of the entire enterprise * * *
>
> Typically, this approach is followed where there is unity in use and management of the enterprise being taxed.

[21]Apparently, its argument was so limited Mobil felt that the prior Supreme Court of Vermont decisions of *Gulf Oil Corporation v. Morrison*, 120 Vt. 324, 141 A.2d 671 (1958); *Woolworth v. Commissioner of Taxes, supra;* and *In Re Goodyear Tire & Rubber Company, Corporate Income Tax 1966, 1967, 1968*, 335 A.2d 310 (Vt. 1975), foreclosed any other commerce clause or due process arguments.



In reversing the decision of the Commissioner, the trial court simply held that the Vermont income tax statute, to the extent it included dividends and interest income in apportionable income, violated what it deemed to be the "multiple risk" doctrine of the commerce clause.[22]

The question before the Vermont Supreme Court for resolution and Mobil's contentions are stated as follows by the Court:

> Mobil does not claim that it was not a taxable corporation during the years in question, nor does Mobil argue that the apportionment formula resulted in too great a percentage of it tax base being subject to taxation in this state. Rather, Mobil objects to its investment income being included in its Vermont tax base at all. Mobil filed tax returns during each of the years in question, determining its tax base by applying the apportionment factor, reckoned according to the statute, to operating income only. That is, in determining its "Vermont net income" for each year, Mobil took its net income for federal income tax purposes and reduced this figure by amounts representing dividend and interest income. This is not authorized by law, and upon audit the Vermont Department of Taxes added the amounts back in and assessed deficiencies. (Juris. St., p. 21a)
>
> * * * * *
>
> The single question presented here is: Does Vermont's application of its apportioned net income tax to the investment income in issue constitute multiple taxation prohibited by the Commerce Clause?
>
> Mobil's argument that Vermont's tax would impose an unconstitutional burden on interstate commerce involves a number of propositions. The first is that taxes subjecting interstate businesses to a

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[22]In so holding, the trial court, as a matter of law, had to assume (1) that the commercial domicile had the power to tax such income in full; (2) that the commerce clause prohibited any risk of multiple taxation of any item of income; and (3) that the "commercial domicile" rule took precedent over the "apportionment rule." The Vermont trial court offered no explanation in support of any of these assumptions.

risk of multiple taxation not borne by interstate business violate the Commerce Clause. The next is that the test of multiple taxation is the power of other jurisdictions to tax rather than the exercise of that power. The last is that the state of a corporation's commercial domicile, in Mobil's case New York, has the constitutional power to tax its corporation's dividend and interest income without apportionment. Mobil argues that if New York has the authority to tax all of Mobil's investment income, there is a risk that it will do so. If Vermont's tax upon a portion of the same income is sustained, there then will be a risk of multiple taxation. If the mere existence of the power is the constitutional test, then an impermissible burden would be shown by establishing New York's right to tax without apportionment. (Juris. St., pp. 22a-23a).

Since the Supreme Court of Vermont did not find that Vermont lacked the constitutional authority to impose a properly apportioned corporate income tax on that part of "federal taxable income" attributable to activities and sources in Vermont, based on such arguments, it reversed the decision of the trial court and upheld the assessments in question.

Mobil here challenges the validity of the decision of the Vermont Supreme Court under the due process and commerce clauses of the U.S. Constitution, although it raised no due process argument before the Vermont Supreme Court.

### B. ANALYSIS OF THE FACTUAL RECORD.

In light of Mobil's arguments, and that of its amicus, it is important to determine the status of the record. Since Mobil has the burden of proof to establish its claim to constitutional immunity, *Norton Co. v. Department of Revenue*, 340 U.S. 534, 537 (1951), the following facts to the extent relevant, must be deemed to be true:

(1) Mobil, for the years in question, conducted an integrated world-wide unitary business with its affiliated and subsidiary corporations and conducted that business, in part, in Vermont for the tax years in question.



(2) The "investments" of Mobil in the stocks in question and the income from these investments were used by Mobil in the furtherance of and in the conduct of its petroleum and petroleum related business, which it conducted in part in Vermont, and these stocks and income therefrom constitute a part of the unitary trade or business of Mobil.[23] (The fact that Mobil does not carry on its unspecified activities concerning its stock "investments" in question in Vermont is irrelevant in regard to the unitary nature of Mobil's business which it apportioned in part to Vermont.)

(3) An appropriate analysis of Mobil's dealings with its wholly owned subsidiaries could reveal that what Mobil received as "dividends," from stock "investments" in fact constituted significant income which should be reclassified as Mobil's "operating income" from its petroleum and petroleum related businesses which it conducted in part in Vermont for the years in question.[24]

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[23]For ought that appears in the record, it could be assumed that Mobil made the stock investments in question and utilized the income from these investments to specifically further the conduct of its business in Vermont. For example, it could be assumed that it created its wholly-owned subsidiaries of Mobil Marine Transportation, Ltd., Mobil Oil Iraq with limited liability and Pegasus Overseas, Ltd., from which it received substantially all of the dividend income in question in furtherance of its petroleum and petroleum related marketing activities in Vermont.

[24]This statement may be illustrated by the following hypothetical example. Assume that Corporation A manufactures patented widgets and sells them to Corporation B, a wholly owned subsidiary, at or near cost. Corporation B in turn sells them at a substantial profit and returns that profit to Corporation A in the form of "dividends." Obviously what should be truly classified as "dividend" income of Corporation A and income from Corporation A's manufacture of widgets cannot be ascertained. Any such simplified picture would be compounded if there were various other unitary ties between Corporation A and Corporation B and if the income from Corporation B's sale of the widgets was filtered through a large number of subsidiary corporations of Corporation A (as well as subsidiary corporations of such subsidiaries) that performed vertically integrated operations in the production, financing, development and marketing of widgets.

(4) The fact that Mobil's first tier subsidiary and affiliated corporations do no business in Vermont and derive unsubstantial amounts of income from "sources" within the United States does not establish their subsidiary and affiliated corporations do not do so.[25]

The presumed facts that Mobil, together with its world-wide subsidiary and affiliated corporations, is conducting a fully integrated international petroleum and petroleum related business, is substantiated by (1) Mobil's consolidated annual reports and financial and operating statistics for the years 1970, 1971 and 1972 (Exhibits 9-14 to the Stipulation); (2) various public reports, such as Mobil's *Form 10-K Annual Reports* filed with the Federal Securities and Exchange Commission; and (3) the information pertaining to Mobil published in the authoritative *Moody's Industrial Manual.*

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[25]For example, Corporation A may have a subsidiary Corporation B that conducts all of its business activities of producing crude oil in Canada which Corporation B in turn sells to its own subsidiary, Corporation C for refining and sale in the United States, including the state of Vermont. Under such circumstances, Corporation B does not have any United States source income unless it maintains a "permanent establishment" in the United States. Yet, it is obvious that this is not true as to its subsidiary, Corporation C.

The type of factual pattern in the above example can be illustrated by *Appeal of Texaco, Inc.* (Calif. State Bd. of Equal. decision of January 11, 1978; CCH Cal. Rpts. ¶ 205-821). In that case, a wholly-owned subsidiary of Texaco, as contemplated by a consortium agreement by eight oil companies (apparently including Mobil, see p. 1, 1972 10-K report of Mobil), was formed as a paper corporation to hold Texaco's interests under the agreement and to purchase oil from the National Iranian Oil Company for 12½% of the posted price. This subsidiary in turn sold the oil at the "posted price" to another wholly-owned subsidiary of Texaco that in turn sold the oil at a loss on the world market. If the second subsidiary had been formed by the first subsidiary as a second tier corporation and if the second tier corporation did business in the United States and Vermont, the *Texaco* example would conform to our hypothetical example.

As to the nature of the problems posed by the foregoing example, see a note entitled: "Multinational Corporations and Income Allocation Under Sec. 42 of the Internal Revenue Code," 89 Harv. L. Rev. 1202 (1976).



As indicated in *Moody's* for 1972:

"The company [Mobil Oil Corporation], together with subsidiaries and affiliates, is a fully integrated international oil company, having crude oil production, pipeline and marine transportation facilities, refineries and wholesale and retail distributing stations and equipment. (Bracketed material added)

* * * Products are sold in more than 100 countries in the free world. Mobil also manufactures and sells a wide range of chemicals." (Moody's Industrial Manual, 1972, p. 117)

As set forth in Mobil's 10-K Report for 1972, p. 1:

"Mobil Oil Corporation, one of the major international oil companies, was incorporated in the State of New York in 1882. The corporation conducts an integrated business in the production, transportation, refining, and marketing of petroleum and natural gas and products thereof, and in the manufacture and marketing of chemicals."

What Mobil means by this statement in its 1972 10-K Report is expanded in considerable detail in its Annual Reports to its stockholders. (Exs. 9-11 to the "Stipulation of Facts") It is also substantiated by the testimony of William P. Tavonlareas, President of Mobil Oil Corporation, before the Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary, United States Senate, Washington, D.C., January 21, 1976, in opposition to divesture of the major oil companies.

By far the largest single payor of dividend income to Mobil for the years in question, was Mobil Marine Transportation, Ltd. (Ex. 8, A75) "Transportation" of Mobil is graphically illustrated and commented upon on pages 8-11 of its 1972 Annual Report to stockholders. Mobil there noted the economy of size and the utilization of its ships in United States coastal trade. It offered the following comment on page 10:

"In the United States, we are taking part in studies to determine the feasibility of constructing vlcc (very large crude carriers) travel on the gulf and east coast.

> At present, no U.S. port can accomodate a full loaded vlcc. As the abundance of imported oil grows, larger terminals will be increasingly needed to handle them economically."

Again, in commenting on its exploration and producing activities in its 1972 Annual Report to stockholders at pages 4-7, Mobil indicates the world-wide integrated nature of its activities and its "investments" in this regard.

Nowhere in the foregoing reports is there any indication that Mobil as a parent is engaged in any investment activities as a "holding company" or in any investment activities apart from its petroleum and petroleum "related business." In fact, on page F-1 of its 1972 10-K report, it stated:

> "Individual financial statements of the Corporation [Mobil] have been omitted because (a) the Corporation is primarily an operating company and (b) the Corporation owns substantially all of the equity securities of and has guaranteed substantially all of the debt of its consolidated subsidiaries."

In regard to the dividends in this cause, as indicated by Ex. 8 (A75-A78), the great bulk of the dividend income in question, which Mobil labeled as "foreign source dividend income" (what Mobil means by "foreign source" is undefined in this record), was received by Mobil from three wholly-owned foreign incorporated subsidiaries and from its 10% interest in the Arabian-American Oil Company (ARAMCO). The dividend income from these corporations for the years in question compared to the total dividend labeled as "foreign source dividend income" on Exhibit 8 is as follows:



| COMPANY | AMOUNT OF DIVIDEND | | | DIVIDEND TOTALS |
|---|---|---|---|---|
| | **1970** | **1971** | **1972** | **1970-1972** |
| Mobil Marine Transportation, Ltd. | 49.6 | 151.8 | 167.4 | 368.8 |
| Mobil Oil Iraq with Limited Liability | 45.0 | 71.2 | 51.3 | 167.5 |
| Pegasus Overseas, Ltd. | 51.0 | 25.2 | 8.9 | 85.1 |
| ARAMCO** | 1.7 | 1.8 | 25.5 | 29.0 |
| Subtotal | 147.3 | 250.0 | 253.1 | 650.4 |
| All Others | 26.7 | 32.4 | 26.8 | 85.9 |
| Total | 174.0 | 282.4 | 279.9 | 736.3 |
| % of Total | **84.7%** | **88.5%** | **90.4%** | **88.3%** |

*To closest 1/10 of million dollars.
**Includes only 15% of ARAMCO dividends because only 15% were included in federal taxable income and thus, in income subject to apportionment under Vermont law.

While the record is silent as to the nature of the activities of these subsidiary corporations and their relationship to Mobil's unitary petroleum business, it is fair to assume that they and their subsidiaries and affiliates are involved in worldwide production and transportation of petroleum and petroleum related products.[26]

The foregoing assumptions pertaining to the integrated nature of Mobil's business with that of its affiliated and subsidiary corporations is substantiated also, as to prior years, by its pleadings filed in proceedings before the Corporation Tax Appeal Board of the State of Michigan in Docket Nos. 59-5 and 60-6, which involved the Michigan Corporate "net worth" franchise tax. Mobil, in its Amended Complaint in Docket No. 59-5, sworn to by its Assistant Treasurer, alleged as follows:

*FOUR:* Throughout the calendar years 1952 and 1957, inclusive (which are the base years by reference to which

[26]These corporations, as well as other subsidiaries of Mobil, are so integrated with Mobil's reports and financial statements, there is no way to identify them apart from Mobil in any respect whatsoever.

the tax liability for the respective tax years 1953 and 1958, inclusive, is determined, such years being hereinafter referred to as "base years"), the facts upon which appellant relies in support of this appeal were as follows:

1. Appellant was a New York corporation maintaining its principal and executive offices in New York City, from which it operated an integrated worldwide oil business as a producer, refiner, transporter, and marketer of crude petroleum and its refined products. It operated directly through divisions and branches in some states, including Michigan, but in other states and in almost all of its far-flung worldwide operations, the business was conducted through subsidiary and affiliated corporations. * * *

Appellant further specifically alleges the fact to be that during the period involved, the consolidated group (comprising the parent company and all of its subsidiaries and affiliates) constituted one organic, functional whole; and that each subsidiary and affiliated company and the consolidated group (comprising the parent company and its subsidiary and affiliated companies) as a whole derived economic strength and power from appellant's centralized supervision, management, and control, as will be more fully shown by evidence at the hearing.

2. During the base years, appellant had substantial interests in subsidiary and affiliated companies, upwards of 43% of appellant's total assets (subject to some normal variation from year to year) consisting of its investments in its subsidiaries and affiliated companies.

3. In the operation of the petroleum business, the four major functions consist of (a) exploration for and production of crude oil, (b) refining of crude oil into products, (c) marketing either crude oil or products, and (d) transportation of crude oil or products by pipeline, ship, or wheeled vehicle. The parent company and its subsidiaries and affiliates engage in the performance of these four functions in the manner hereinafter described. Each of the subsidiaries and affiliates is engaged in some



phase of the producing, transporting, manufacturing, or marketing of petroleum or petroleum products.

(a) Exploration and production. The parent company did not, during the period here involved, engage in any exploratory operations nor in the production of crude oil either in foreign countries or in the United States (except for an operation in the State of Michigan producing approximately 200 barrels a day). The primary source of "domestic" crude oil (i.e., crude oil produced in Canada) for the parent company and for those of its subsidiaries engaged in the operation of refineries in the United States, is by purchase from four subsidiaries, three in the United States and one in Canada. * * * "Foreign" crude oil (i.e., crude produced outside the United States or Canada) used by the parent company and by those of its subsidiaries engaged in the operation of "Socony" refineries in the United States was obtained principally by purchases made by the particular company from foreign producers. Such purchases were made by the parent company both for refineries operated by it and for refineries operated by some of its subsidiaries in the United States. A large percentage of the "foreign" crude oil used in "Socony" refinery operations in the United States by the parent company or its subsidiaries was supplied by a subsidiary engaged in production of crude oil in South America, Mobil Oil Company de Venezuela, and the wholly-owned subsidiary of an affiliate simiarly engaged, Colsag Corporation. Such sales by these companies accounted for the equivalent of an average of approximately 64% of the crude oil sold by these companies.

(b) Refining. Appellant and its subsidiary and affiliated companies engaged also in the refining of oil. * * * The parent company prescribed formulae, specifications and standards which were conformed to in all refineries operated by it or by its subsidiary or affiliated companies. The parent company conducted refinery research, the results of which were made available to all the refineries operated by subsidiary and affiliated

companies, and the cost of the research was shared by the subsidiary and affiliated companies. The parent company sent technical advisors to all of the refineries operated by it, its subsidiaries, and its affiliates. Patented processes owned by the parent company were made available for use at and were used at refineries operated by subsidiary and affiliated companies. Conversely, manufacturing techniques perfected at refineries operated by subsidiary or affiliated companies were made available for use at and were used at refineries operated by the parent company and by other subsidiary and affiliated companies.

(c) Marketing. Petroleum products produced at refineries operated by the parent company and its domestic subsidiaries were marketed under brand names owned by the parent company, selected by the parent, and identifying the product of a product of appellant, e.g., "MOBILGAS," "MOBILOIL" and "MOBILHEAT" fuel oil. Uniform sales manuals were utilized by all United States divisions and by all United States subsidiaries. National advertising campaigns supported marketing programs of both the parent company and its United States subsidiaries, all of which contributed to the cost of such campaigns. The parent company exercised general superintending control over the marketing of the products (many of which are known by the same "MOBIL" trade name) of its subsidiaries and affiliates in foreign countries. Sales manuals were furnished to foreign subsidiaries and affiliates as prototypes to be translated into the appropriate foreign language and modified to conform with local sales customs and practices.

(d) Transportation. Transportation of crude oil and petroleum products between foreign subsidiaries and affiliates was accomplished principally by fleets of vessels operated by a wholly-owned subsidiary, Mobil Shipping Company, Ltd., and by an affiliated company, Standard-Vacuum Oil Company, Inc., and its subsidiaries. Transportation of "foreign" crude oil to this country, for use in refineries operated by the parent company and its United States subsidiaries, was accomplished principally through



a fleet of vessels operated by another wholly-owned subsidiary, Mobil Tankers Company, SA. Transportation of petroleum products in U.S. coastal and inland waters was accomplished by use of a fleet of coastwise ships and inland floating equipment operated by the marine division of the parent company. All of the United States subsidiaries relied exclusively on the parent company for the importation of their supplies of foreign crude oil; and they relied principally on the parent company for the coastwise distribution of petroleum products. Within the United States, overland transportation of crude oil by the parent company and all of its United States subsidiaries was accomplished in large measure by pipelines owned and operated by the parent company and its subsidiaries. All of the pipelines were available for the use of all subsidiaries.

* * * * *

5. As above specified with reference to the principal and typical subsidiary and affiliated companies, appellant further shows and will establish by proof that the function of each and all of its other subsidiary and affiliated companies was to perform one or more of the required steps in the processing of oil from the underground reservoirs in which it is found to sale to the ultimate consumer under a brand name. The operations of each of the subsidiary and affiliated companies was closely integrated with those of the parent company in the manner hereinafter more particularly specified, viz.:

(a) The parent company in its New York headquarters maintained daily communication with each of the subsidiary and affiliated companies to assure prompt exchange of financial and operational information between all units comprising the consolidated group (i.e., the parent company, its subsidiaries and its affiliates).

(b) The parent company conducted teachnical research and engineering studies relating to refining processes, operations, products, and marketing; and the parent company advised all subsidiaries and affiliated companies of the results thereof.

(c) The parent company and its subsidiary and affiliated companies followed standardized accounting and financial reporting procedures; and the parent company's representatives periodically reviewed the adequacy of these procedures with its subsidiary and affiliated companies in the field.

(d) The financial statements of the parent company and its subsidiaries were consolidated into a single statement for purposes of financial analyses and reports to appellant's stockholders.

(e) The parent company made the initial determination of the financial needs of its subsidiaries.

(f) All subsidary and affiliated companies regularly reported the results of various aspects of their operations to the parent company.

While it is recognized that pleadings in another proceeding for prior years does not establish any facts in this cause, we believe that the foregoing illustrates the reasonableness of the conclusion, when coupled with the other documents referred to herein, that Mobil's "investments" in its subsidiary and affiliated corporations were "investments" in the furtherance of its unitary integrated worldwide petroleum and petroleum related business and that its activities associated with those "investments" were not limited to an investor's management of stocks.

## SUMMARY OF ARGUMENT

Beginning with the early property tax case of *Adams Express Co. v. Ohio State Auditor,* 165 U.S. 194 (1896), rehearing 166 U.S. 185 (1897) down to *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 (1978), this Court has uniformly sustained reasonably apportioned state imposed property, franchise or net income taxes. In sustaining these taxes against due process or commerce clause objections, it has never limited the apportionable tax base to in-state values, properties or income. In the application of apportionment formulae in income tax cases, this Court has uniformly held that the states are free to use the "unitary business"



technique even if some components of the unitary business are located outside the taxing jurisdiction. *U.S. Steel Corp. v. Multistate Tax Commission,* 434 U.S. 452 at 473, footnotes 25 and 26; *Underwood Typewriter Co. v. Chamberlain,* 245 U.S. 113 (1920); *Bass, Ratcliff & Gretton Ltd. v. New York Tax Commission,* 266 U.S. 271 at 282 (1924); *Butler Bros. v. McColgan,* 315 U.S. 501 (1942). It has recognized that "net income taxes," unlike gross receipts taxes, are not imposed on any transactions from which net income may be derived. *Peck & Co. v. Lowe,* 247 U.S. 165 (1918). Thus, "Neither the privilege nor the burden is affected by the character of the source from which the income is derived. For that reason income is not necessarily clothed with the tax immunity enjoyed by its source." (*N.Y. ex rel. Cohn v. Graves,* 300 U.S. 308 at 312 (1936) It has upheld unitary apportionment even though applied to income from foreign activities of a foreign corporation which earned no taxable income in the United States for federal income tax purposes. *Bass, Ratcliff & Gretton, supra.* Furthermore, this Court has recognized that the possession of large blocks of intangible properties gives a business a value, in conducting instate activities, which can be considered in imposing a state tax on such activities. *Flint v. Stone Tracy Co.,* 220 U.S. 107 at 166); *Ford Motor Co. v. Beauchamp,* 308 U.S. 331 at 336 (1939), citing *Bass, supra,* and *National Leather Co. v. Massachusetts,* 277 U.S. 413 (1927). It has also held that it is presumed that all of the properties of a corporation contribute to the operations of its business as a whole and the burden is on the taxpayer to prove otherwise. *Adams Express Co. v. Ohio State Auditor,* 165 U.S. 194 at 227 (1896). It has rejected the argument that intangibles associated with a unitary business should be attributable solely to the commercial domicile. *Adams Express Co. v. Ohio State Auditor,* rehearing 166 U.S. 185 at 218). This Court has appropriately held that an apportionment formula is only a rough approximation of income attributable to the taxing jurisdiction and that an

apportionment formula does not purport to identify or tax any income derived from specific sources. *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 at 278-280 (1978). It has thus invalidated an apportionment formula only when the taxpayer has established by clear and cogent evidence that the formula resulted from the taxation of income or values which could not be reasonably attributed to the taxpayer's properties or activities within the state. *Norfolk & Western Ry. Co. v. North Carolina,* 297 U.S. 682 (1968); *Hans Rees' Sons, Inc. v. North Carolina,* 283 U.S. 123 (1931).

While this Court has repeatedly held that the purpose of the commerce clause was to prevent any undue multiple burden on interstate commerce, it has also uniformly held that any prohibited risk of multiple taxation is satisfied by reasonable apportionment rules. *Northwest Portland Cement Co.,* 358 U.S. 450 at 448, 449 (1959); *Japan Line Ltd. v. County of Los Angeles,* ____ U.S. ____ (decided April 30, 1979). It has also refused to engage in hypothetical speculation in resolving any alleged multiple taxation question. *Northwest Portland Cement Co., supra; Standard Pressed Steel Co. v. Dept. of Revenue,* 419 U.S. 506 (1975); *International Harvester Co. v. Dept. of Treasury,* 322 U.S. 340 at 348 (1944); *Northwestern Airlines v. Minnesota,* 322 U.S. 292 at 295 (1944); *Moorman Mfg. Co. v. Bair,* 437 U.S. 267 at 276 (1977); *First Federal S & L v. Massachusetts Tax Comm'n,* 437 U.S. 255 at 262, footnote 9 (1977).

Though different state income attribution rules potentially may result in either undertaxation or overtaxation of income of a multistate-multinational corporation, this Court has refused to interpret the commerce clause as requiring judicially prescribed uniform division of income rules. The proscription of such uniformity involves complex questions which require political, not judicial, resolution. *Moorman, supra,* at 437 U.S. 278-280.

In sum, this Court has concluded that if a state tax is fairly apportioned and non-discriminatory and if it is



applied to an activity with substantial nexus in the state and if it is designed to reasonably compensate the state for services provided, a state tax does not controvene either due process clause (*Moorman, supra,* 437 U.S. 272) or commerce clause (*Japan Line, supra,* Slip. Op. p. 10) limitations on state taxing power.

Notwithstanding these well-established constitutional principles, Mobil and its amicus curiae here contend that Vermont's generally accepted and well-recognized three-factor apportionment formula as applied to Mobil's "federal taxable income" is unconstitutional under both the Due Process and Commerce Clauses of the Constitution of the United States, even though there is no claim that it arrives at an unreasonable result or is applied to nonunitary income. They premise this novel argument on a series of invalid and unsupported factual conclusions and legal assumptions.

They premise their due process arguments on the erroneous legal assumption that Vermont, in including Mobil's dividends in apportionable net income, has imposed a tax on these dividends and on the unsubstantiated factual conclusion that Mobil's stock holdings are unrelated to Mobil's business operations which it conducted in part in Vermont.

However, the fact that Mobil's stock holdings and dividends therefrom are located and managed from without Vermont and the fact that Mobil's legal and commercial domicile is without Vermont does not support the conclusion that its stock holdings and dividends therefrom were not connected with its unitary petroleum and petroleum related business conducted in part in Vermont. Neither does the fact that Mobil's dividends were included in Vermont's income tax base which was subject to apportionment support the argument that Vermont is attempting to tax its dividend income or "foreign commerce."

Inasmuch as the conclusion of an item of income in apportionable income is not the taxation of that item, and inasmuch as Mobil conducted substantial business

operations in Vermont which has not been shown to be disassociated from its stock holdings and its dividends derived therefrom, and inasmuch a Mobil has not shown that Vermont has taxed any income not rationally related to values connected with its Vermont business activities, Mobil's due process argument is frivolous.

As in their due process arguments, Mobil and its amicus premise their foreign commerce argument on invalid assumptions and contentions, including those relied on in support of their due process argument. However, Vermont, by applying its apportionment formula to Mobil's "federal taxable income," is no more subjecting to tax Mobil's dividend income than it is subjecting to tax Mobil's income from its out-of-state refining, producing, marketing and transporting operations. All that Vermont has taxed in this case is an unidentifiable portion of Mobil's income which can be reasonably attributable to its Vermont business by a reasonable and generally accepted three-factor apportionment formula.

Mobil and its amicus assume that the inclusion of dividends in apportionable income of a domestic United States corporation is a tax imposed on "foreign commerce." This argument again disregards the nature and incidence of Vermont's corporate income tax law and the operation and effect of its apportionment formula. Furthermore, even if Vermont in fact taxed Mobil's dividends from its foreign subsidiaries, which is not the case, still it would not be a tax on Mobil's conduct of "foreign commerce." The inclusion in apportionable income of dividends of a domestic U.S. corporation which it derives from its domestic ownership and management of stock in foreign corporations does not constitute the taxation of its foreign operations. This fact, coupled with the fact that Vermont does not seek to tax such dividends, destroys Mobil's "foreign commerce" argument.

Furthermore, in advancing its "foreign commerce" argument, Mobil erroneously argues that *Japan Line Ltd.*



*v. County of Los Angeles, supra,* is controlling and that *Moorman Mfg. Co. v. Bair, supra,* is not. However, this Court in *Japan Line* carefully limited the additional foreign commerce clause standards there enunciated to foreign corporations engaged solely in international commerce. It there found that any undue risk of state multiple taxation of domestic corporations could be policed by appropriate application of apportionment principles, which was not possible in regard to foreign corporations. It thus limited the *Japan Line* property tax domicillary rule to foreign-owned instrumentalities of commerce which were used exclusively as instruments of foreign commerce. As to interstate instrumentalities of domestic corporations, it affirmed the principle of full apportionment. Thus, *Japan Line* is totally irrelevant here.

Equally untenable is the argument of Mobil and its amicus that the principles affirmed by this Court in *Moorman* and reaffirmed in *Japan Line* applicable to domestic corporations engaged in interstate commerce are not controlling. In order to distinguish *Moorman,* they argue that there is a constitutional difference between this Court's refusal in *Moorman* to prescribe uniform apportionment formulae and for it to interpret the commerce clause to mandate specific allocation of dividend income to the commercial domicile. This Court in *Moorman* aptly noted that any constitutional prescription of a uniform apportionment formula was inexorably tied to other income attribution rules. *Moorman, supra,* at 437 U.S. 278-279. This fact was significant to its refusal to invalidate Iowa's single-sales-factor apportionment formula. Since, as a matter of fact, an apportionment rule and what is subject to apportionment are but two sides of the same coin, there is no difference between the two in a constitutional sense. In substance, then, Mobil and its amicus are requesting this Court to overrule *Moorman* by their back door approach to the fundamental constitutional question decided in *Moorman,* namely, whether this

Court of Congress, to the extend needed, should prescribe uniform division of income rules.[27]

Mobil and its amicus also assume (1) that the risk of multiple taxation is not constitutionally satisfied, as to domestic corporations, by reasonable apportionment rules; and (2) that taxation of dividends (and ostensibly all income from intangibles) solely by the commercial domicile better serves the alleged "multiple risk" commerce clause limitation than does reasonable apportionment rules. The first assumption is contrary to the express holdings of this Court. Irrespective of the otherwise validity of Mobil's "multiple risk" argument, this Court has uniformly held that any "multiple risk" in a constitutional sense is satisfied by reasonable apportionment standards. The second assumption is based on the unsubstantiated factual conclusion that differences in income attribution rules which are currently utilized by the states exposes dividend income to a risk of overtaxation rather than undertaxation. This is a surprising argument for Mobil to advance in this cause when the existing state attribution rules, however construed, result in substantial undertaxation of its income. Neither Mobil nor the C.O.S.T. members have asserted or sought to prove that they are exposed to a risk of multiple taxation under existing state attribution rules as applied to their dividends from their foreign subsidiary and affiliated corporations. They simply ask this Court to assume, as an abstract proposition, that differences in

[27]While Mobil and its amicus would limit *Moorman* to the validity of an apportionment formula, they ignore the fact that the question here involves the validity of Vermont's apportionment formula. The fact that they attack the apportionment formula result by reference to the apportionable income rather than by reference to the factors employed is a difference without substance. An apportionment formula may be invalid as applied to any taxpayer only if the interrelationship between the apportionable tax base and the apportionment formula produce an unconstitutional result. Thus, in *Butler Bros. v. McColgan, supra,* this Court considered both the reasonableness of the apportionment formula to assign income and the income base to which it was applied. (315 U.S. 507-508)



state attribution rules establishes a risk of multiple taxation as a matter of law. It has consistently refused to so speculate.

Mobil's argument that the Vermont tax is incompatible with federal policy regulating foreign commerce is subject to the same basic defects as its other "foreign commerce" arguments. There is absolutely no constitutional basis for Mobil and its amicus to conclude, based on *Japan Line,* that state taxation of income of domestic U.S. corporations, which is included in federal taxable income, must yield, by analogy, to complex, vaguely defined federal tax policies which have been formulated by the federal government solely for federal income tax purposes. State income taxation, whether in the context of income attribution rules or otherwise, is not the subject matter of either the Internal Revenue Code or federal tax treaties unless they expressly so provide. The sole issue here, then, "Whether this Court should constitutionally mandate a "separate accounting" domiciliary rule for state income taxation of dividends, to the exclusion of reasonable apportionment of this income by the application of unitary principles," is totally unrelated to any federal international policy concerns such as those involved in *Japan Line.* Also, Mobil has not established any federal policy which in any manner controls disposition of this case. Nor has it shown that any such assumed policy is better served by taxation of dividends from foreign subsidiaries by the state of commercial domicile rather than by apportionment to the states in which multinational corporations conduct their unitary business operations.

From the foregoing, the unitary principles embodied in the apportionment decisions of this court control disposition of this case. When properly applied to the facts and circumstances of this case, these principles indicate that this Court should affirm the decision below of the Supreme Court of Vermont.

## ARGUMENT

### I.

### It is Readily Apparent That Mobil's Due Process Argument is Frivolous Inasmuch as Mobil Has Failed to Prove That the Vermont Apportionment Formula as Applied to Its Federal Taxable Income Does Not Reasonably Measure Its Income it Derived From Its Business Operations in Vermont or That the Dividends in Question and the Income Derived Therefrom Were Disassociated From Its Unitary Business Which It Conducted Both Within and Without Vermont, and Inasmuch as Vermont Can Take Into Consideration Out-of-State Properties, Activities and Income in Arriving at a Reasonable Apportionment of the Unitary Income of a Trade or Business.

The general due process standard applicable to an apportioned state income tax is stated as follows in *Northwestern States Portland Cement Co.*, 358 U.S. 450:

> "Nor will the argument that the exactions contravene the Due Process Clause bear scrutiny. The taxes imposed are levied only on that portion of the taxpayer's net income which arises from its activities within the taxing State. These activities form a sufficient 'nexus between such a tax and transactions within a state for which the tax is an exaction.' *Wisconsin v. J.C. Penney Co., supra*, at 445. * * * The record is without conflict that both corporations engage in substantial income-producing activity in the taxing States. * * * As was said in *Wisconsin v. J.C. Penney Co., supra*, the 'controlling question is whether the state has given anything for which it can ask return.' Since by 'the practical operation of [the ] tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred * * *' it 'is free to pursue its own fiscal policies, unembarrassed by the Constitution * * *' *Id.*, at 444." (358 U.S. at 464, 465)

As otherwise stated in *Moorman:*



> "The Due Process Clause places two restrictions on a State's power to tax income generated by the activities of an interstate business. First, no tax may be imposed unless there is some minimal connection between those activities and the taxing State. *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753, 756. * * * Second, the income attributed to the State for tax purposes must be rationally related to 'values connected with the taxing state.' *Norfolk & Western R. Co. v. Missouri*, 390 U.S. 317, 325." (437 U.S. 267 at 272-273)

Notwithstanding the fact that its activities in Vermont clearly exceeded any due process nexus requirements and notwithstanding the fact that the income subject to tax was reasonably related to Mobil's Vermont activities, Mobil attempts to attribute its gross dividends in question to out-of-state sources for due process purposes.

In so doing, it relies on two faulty premises, namely, (1) that Vermont is imposing an income tax on its dividend income and its stock holdings in its foreign subsidiary and affiliated corporations and its out-of-state activities in regard thereto; and (2) that the income derived therefrom is totally disassociated from and unrelated to its Vermont business activities and operations. Neither of these propositions is true. Furthermore, even if they were, so long as Vermont's apportionment formula attributed to Vermont only income that is reasonably related to a measure of Mobil's activities conducted within Vermont, there is no merit to Mobil's due process argument.

The fact that income or properties is included in the tax base subject to apportionment which by "separate accounting" would be attributable to out-state sources and activities has never triggered invalidation of an apportionment formula, so long as the taxpayer has not shown that the apportionment result reached extra-territorial values or income. *Butler Brothers v. McColgan*, 315 U.S. 501, (1942).

In contending that Vermont is attempting to tax its dividend income derived from out-of-state activities or sources, Mobil misconstrues the operative effect of the formula method of computing taxable income. In answering Moorman Manufacturing Co.'s argument that the Iowa single-sales-factor apportionment formula sought to tax income attributable to Moorman's manufacturing operations in Illinois, this Court stated in *Moorman:*

> "Since 1934 Iowa has used the formula method of computing taxable income. *This method, unlike separate accounting, does not purport to identify the precise geographical source of a corporation's profits;* rather, it is employed as a rough *approximation of a corporation's income that is reasonably related to the activities conducted within the taxing State.* The single-factor formula used by Iowa, therefore, generally will not produce a figure that represents the actual profits earned within the State. But the same is true of the Illinois three-factor formula. Both will occasionally over-reflect or under-reflect income attributable to the taxing State. Yet despite this imprecision, the Court has refused to impose strict constitutional restraints on a State's selection of a particular formula. See, *e.g., Underwood Typewriter Co.* v *Chamberlain,* 254 U.S. 113; *Bass, Ratcliff & Gretton v. State Tax Commission,* 266 U.S. 271; *Ford Motor Co. v. Beauchamp,* 308 U.S. 331. (Emphasis added; 437 U.S. 267 at 273)

Thus, Mobil's due process of law argument must be rejected because it has not sustained its burden of establishing that its stock holdings in question and its income therefrom were not related to and did not contribute to that part of its business which it conducted in Vermont.

Even if Mobil's argument that the stocks and dividends in question were totally unrelated to its unitary business operations which it conducted in part in Vermont, there is still a serious question as to whether there is any merit to its due process argument. For, Vermont does not seek to tax any of these dividends and



Mobil has not shown that the income attributed to Vermont by the apportionment formula was not "rationally related to 'values connected with the taxing *state'—Norfolk & Western R. Co. v. State Tax Comm'n,* 390 U.S. 317, 325." (*Moorman,* 437 U.S. 267 at 273)[28]

What Mobil and its amicus completely ignore, in both their due process and commerce clause arguments is that *unitary apportionment* principles—*not "separate accounting"* source principles—without exception, when a state seeks to tax integrated business operations which are conducted both within and without its borders. They argue that "separate accounting" rules are relevant within the limited context of the attribution of Mobil's dividend income in question and that apportionment unitary rules otherwise apply. This is an inappropriate, hybrid method of attributing income to either Mobil's Vermont income sources or income producing activities. If Mobil had "separately accounted" for its Vermont income or even for the income from its marketing business which it conducted in part in Vermont, the results would undoubtedly be entirely different that the results Mobil and its amicus contend for here.

As indicated in an article entitled "Recent Developments in State Tax Apportionment and the Circumscrip-

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[28]In *Albany International Corp. v. Halperin,* 388 A.2d 901 (Me. 1978), the Supreme Court of Maine held that interest, capital gains, royalties and income derived from divisions of Albany International which conducted no activity in Maine were subject to apportionment if properly classified as business income under section 1(a) of UDITPA. Since it determined that an apportionment formula renders irrelevant the actual source of business income, the Maine Court refused to construe UDITPA to provide for the apportionment of only that portion of business income which was connected with business transacted in the taxing state. However, in the instant case, we need not cross this bridge. We premise our argument here on the proposition that Mobil has not sustained its burden of proof to establish either (1) that the income and stock in question were unrelated to its unitary business which it conducted in part in Vermont; or (2) that, apart from unitary principles, Vermont has attributed to Mobil's Vermont activities income which is not rationally related to income Mobil derived from its Vermont activities.

tion of Unitary Business," by Jerome R. Hellerstein, XXI National Tax Journal 487, 496:

> "The underlying justification for applying an apportionment formula to the overall tax base of a multistate business is that there exists a unitary enterprise being carried on in more than one state. The formula is a device for attributing to the taxing state its share of the overall tax measure that admittedly is attributable only in part to the state. This principle extends, at lease in a good many states, both to the branches of a single corporation and to subsidiaries and affiliated corporations that are a part of the enterprise. By applying the typical three factor formula, the property, receipts and payroll ratios of all branches, subsidiaries and affiliates are taken into account in determining apportionment ratios, which are then applied to the tax base of the entire business.
>
> [A]t the center of many of the cases, the crucial controversy has been the delineation of the contours of a unitary business." (Footnotes omitted)

Starting with the early utility property tax cases, this Court has uniformly upheld the apportionment of the entire properties, values or income attributable to a unitary business by an apportionment formula which has not been demonstrated by the taxpayer by clear and cogent evidence to tax extraterritorial income or values.

In *Adams Express Co. v. Ohio State Auditor,* 165 U.S. 194 (1896), this Court summarized the holdings of its prior utility property tax decisions pertaining to unitary reporting as follows:

> "As to railroad, telegraph and sleeping-car companies, engaged in interstate commerce, it has often been held by this Court that their property in the several states through which their lines or business extended might be valued as a unit for purposes of taxation, taking into consideration the uses to which it was put and all the elements making up aggregate value, and that a portion of the whole fairly and properly ascertained might be taxed by the particular state, without violating any federal restrictions. [Cases cited.] The valuation was, thus, not confined to the



> wires, poles, and instruments of the telegraph company; or the roadbed, ties, rails and spikes of the railroad company; or the cars of the sleeping-car company, but included the proportionate part of the value resulting from the combination of the means by which the business was carried on, a value existing to an appreciable extent throughout the entire domain of operation." (165 U.S. 220, 221)

In the *Adams Express Co.* case, this Court went on to hold that all of the property of the express company which was used in its trade or business, including its intangible assets, were properly subject to apportionment for ad valorem property tax purposes. Furthermore, this Court there held that:

> "There is here no attempt to tax property having a situs outside of the state, but only to place a just value on that within. Presumptively, all the property of the corporation or company is held and used for the purposes of its business, and the value of its capital stock and bonds is the value of only that property so held and used.
>
> "Special circumstances might exist, as indicated in *Pittsburg C. C. & St. L. R. Co. v. Backus,* 154 U.S. 421, 443 [38: 1031, 1044, 4 Inters. Com. Rep. 677], which would require the value of a portion of the property of an express company to be deducted from the value of its plant as expressed by the sum total of its stock and bonds before any valuation by mileage could be properly arrived at, but the difficulty in the cases at bar is that there is no showing of any such separate and distinct property which should be deducted, and its existence is not to be assumed. It is for the companies to present any special circumstances which may exist, and, failing their doing so, the presumption is that all their property is directly devoted to their business, which being so, a fair distribution of its aggregate value would be upon the mileage basis." (167 U.S. 227)

This Court therefore concluded in the *Adams Express Co.* case that the total market value of the stock of the express company could be taken into consideration in valuing its properties within the taxing state, even

though its intangibles had a specific situs outside the taxing state at the "commercial domicile."

The foregoing conclusion of this Court in the *Adams Express Co.* case was vigorously opposed by the Company in a lengthy petition for hearing. The Court granted the rehearing and issued its opinion in accordance therewith in *Adams Express Co. v. Ohio State Auditor*, 166 U.S. 185 (1897). In the rehearing, the Express Company objected to including its intangible properties as part of the value subject to apportionment and taxed in part by the State. In holding that the intangible properties (which constituted three-fourths of the total value of the Express Company's capital stock) could be subject to taxation by the apportionment method, this Court reasoned as follows:

> "Where is the situs of this intangible property? Is it simply where its home office is, where is found the central directing thought which controls the workings of the great machine, or in the state which gave it its corporate franchise; *or is that intangible property distributed wherever its tangible property is located and its work is done? Clearly, as we think, the latter.* Every state within which it is transacting business and where it has its property, more or less, may rightfully say that the $16,000,000 of value which is (sic) possesses springs not merely from the original grant of corporate power by the state which incorporated it, or from the mere ownership of the tangible property, but springs from the fact that the tangible property it has combined with contracts, franchises and privileges into a single unit of property, and this state contributes to that aggregate value not merely by the separate value of such tangible property as is within its limits, but its proportionate share of the value of the entire property.
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> * * * * *
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> "The burden of the contention of the express companies is that they have within the limits of the State certain tangible property, such as horses, wagons, and so forth; that tangible property is the only property within the State; that it must be valued as other like property, and upon such valuation alone can taxes be assessed and levied against them.
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> "This contention practically ignores the existence of intangible property, or at least denies its liability for taxation." (166 U.S. 218)



It is thus clear that the *Adams Express Co.* cases and cases relied on therein clearly establish a unit rule or unitary concept for state tax purposes and permits a state to determine the instate privilege, property or income by reference to the total privileges, property or income of the multistate business if there is a unitary relationship between the instate activities or property of the business and its total activities or properties everywhere. They also establish the proposition that all of the properties or income of a unitary business are subject to a reasonable rule of apportionment. These cases also support the principle that an apportionment formula applied to the total value and properties of the unitary business is deemed to be reasonable in result and the burden is upon the taxpayer to establish otherwise. They also hold that the commercial domicile has no special claim to tax intangible properties or values connected with the unitary business and that all such values and properties, wherever located, are appropriately included in the tax base subject to apportionment.

The principles of these early "unit rule" cases were subsequently uniformily applied by this Court to corporate "net worth" franchise and income taxes. In the application of the "unit rule" to corporate franchise taxes, this Court in *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911) and *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939) upheld the apportionment of intangible properties and "going concern" values. It there recognized that the existence of intangible properties by large multistate-multinational corporations contributed substantially to their business which they conducted in various states. As there stated:

1. "Nor can it be justly said that investments have no real relationship to the business transacted by a corporation. The possession of large assets is a business advantage of great value; it may give credit which will result in more economical business methods; it may give a standing which shall facilitate purchases; it may enable the corporation to enlarge the field of its activities and in many ways give it business standing and prestige." (*Flint*, 220 U.S. 166)[29]

2. "In a unitary enterprise, property outside of the state necessarily affects the worth of the privileges within the state. Financial power inherent in possession of assets may be applied, with flexibility, at whatever point within or without the state the managers of the business may determine. For this reason, it is held that an entrance fee may be properly measured by capital wherever located. The weight, in determining the value of the intrastate privilege, given the property beyond the state's boundaries, is but a recognition of the very real effect its existence has upon the value of the privilege granted within the taxing state." (*Ford*, 308 U.S. 336)

This Court in *Ford Motor Co., supra*, held that its decisions in *Bass, Ratcliff & Gretton v. State Tax Commission, supra*, 266 U.S. 271 (1924) and *National Leather Co. v. Massachusetts*, 277 U.S. 413 (1927), were directly applicable.

In *Bass, Ratcliff & Gretton v. State Tax Commission, supra*, 266 U.S. 271 (1924), this Court stated:

> "In *Wallace v. Hines*, 253 U.S. 66, 69, it was recognized that a State, in imposing an excise tax upon foreign corporations in respect to doing business within the State, may look to the property of such corporations beyond its borders to 'get the true value of the things within, when they are part of an organic system of wide extent,' giving the local property a value above that which it would otherwise possess, and may therefore take into account property situated elsewhere when it 'can be seen in some plain and fairly intelligible way that it adds to the value of the (property) and the rights exercised in the State.' This is directly applicable to the carrying on of a unitary business of manufacturing and sale partly within and partly without the State."

[29] In *Flint v. Stone Tracy Co.*, the Court further held:

"There is no rule which permits a court to say that the measure of a tax for the privilege of doing business, where income from property is the basis, must be limited to that derived from property which may be strictly said to be actively used in the business. Departures from that rule sustained in this Court are not wanting." (200 U.S. 166)



The unit rule of taxation, which included a reasonable apportionment of intangible properties and intangible values, as developed in the *Adams Express Co.* cases was first applied to taxes on or measured by net income in *Underwood Typewriter Co. v. Chamblerlain, supra*. In the *Underwood* case, a tangible property apportionment factor was used to apportion to Connecticut manufacturing activities "* * * income upon which the corporation is required to pay a tax to the United States." (254 U.S. 117, 118) In challenging the constitutionality of the apportionment formula, the taxpayer contended that the net income included income from intangibles not connected with its Connecticut manufacturing business or properties. (254 U.S. 114-116) In disposing of the taxpayer's arguments, this Court focused its attention solely on the validity of the apportionment result.

Four years later, in *Bass, Ratcliff & Gretton, supra*, this Court held that the world-wide property and income of a British unitary enterprise were a necessary part of the apportionment computations in measuring the true value of its income attributable to New York. The taxpayer was found to be "a British corporation, engaged in brewing and selling Bass's ale" which it imported and sold in New York City and Chicago. (id., at p. 278) It had world-wide net income of $2,185,600, but "the Company, as reported to the United States, had no net income upon which it was subject to a federal income tax." (id., at p. 279) New York imposed a 3% tax which Bass paid under protest.

On appeal, Bass contended that the tax was imposed "upon a portion of its net income derived from business carried on outside of the United States * * *" (id., at p. 280) Bass argued further that the New York tax "* * * imposes a direct burden upon its foreign commerce in violation of the commerce clause of the Constitution." (id., at p. 280) This Court decisively rejected these contentions. It held that Bass "* * * carried on the *unitary* business of manufacturing and selling ale, in which its profits were *earned in a series of transactions* beginning with manufacture in England and ending in sales in New York * * *" (id., at p. 282) Having found Bass to be a unitary business operation, this Court affirmed that a fair measuring of taxes due the State required inclusion of:

> "* * * the property of such corporations beyond its borders to 'get the *true value* of the things within it, when they are part of an organic system of wide extent' giving the local property a value *above that which it would otherwise possess* * * * (id., at p. 282; emphasis added)

Again, in *Butler Bros. v. McColgan*, 315 U.S. 501 (1942), this Court applied the unit rule it had expressed in the *Adams Express Co.* cases, *supra*, and its observations in *Flint v. Stone Tracy Co.*, *supra*, and *Ford Motor Co. v. Beauchamp*, *supra*, in determining the validity of the apportionment result challenged in *Butler Bros.* It there found:

> "One who attacks a formula of apportionment carries the distinct burden of showing by 'clear and cogent evidence' that it results in extra-territorial values being taxed. See *Norfolk & Western Ry. Co. v. North Carolina*, 297 U.S. 682, 688, 56 S. Ct. 625
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> * * * * *
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> "At least since *Adams Express Co. v. Ohio*, 165 U.S. 194, 17 S. Ct. 305, this Court has recognized that the unity of use and management of a business which is scattered through several States may be considered when a State attempts to impose a tax on an apportionment basis.
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> * * * * *



> "We cannot say that property, payroll, and sales are inappropriate ingredients of an apportionment formula. We agree with the Supreme Court of California that *these factors may properly be deemed to reflect 'the relative contribution of the activities in the various states to the production of the total unitary income,' so as to allocate to California its just proportion of the profits earned from this unitary business. And no showing has been made that income unconnected with the unitary business has been used in the formula.*" (Emphasis added, 315 U.S. 507-508)

In *U.S. Steel Corp. v. Multistate Tax Commission*, 434 U.S. 452 (1978), this Court stated:

> "The 'unitary business' techniques involves calculating a corporate taxpayer's net income on the basis of all phases of the operation of a single enterprise (*e.g.*, production of components, assembly, packing, distribution, sales), *even if located outside the jurisdiction.* The portion of that income attributable to activities within the taxing State is then determined by means of an apportionment formula. See, *e.g.*, *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920). (footnote 25, 434 U.S. 473; emphasis added)
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> * * * * *
>
> "Individual States are free to employ the unitary-business standard. *Underwood Typewriter Co. v. Chamberlain, supra;* accord, *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n*, 266 U.S. 271 (1924)." (footnote 26, 434 U.S. 474)[30]

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[30]As noted by the Supreme Court of California, in rejecting the appeal in *John Deere Plow Co. v. Franchise Tax Board*, 38 Cal.2d 214, 238 P.2d 569 (1951), appeal dismissed for want of a substantial federal question, 343 U.S. 939 (1952), formulary apportionment:

> " 'is not framed on the assumption that there must be uniformity of operating revenues and expenses in the relative functions of the various units contributing to the earnings of an integrated, multistate business' and concluded that the attack on the formula by proof of the higher costs and the less profitable nature of the California business misconceives the whole purport of the unit rule of assessment, which rests on the principle that 'where a business is unitary in character, so that its separate parts

In sum, since Mobil carried on substantial income-producing activities in Vermont for the years in question and there is no showing that Vermont has taxed any income not reasonably related and attributable to those activities, its due process argument lacks substance. As the above decisions amply demonstrate, the fact that the Vermont tax base, prior to apportionment, included dividend income from out-of-state properties and activities is totally irrelevant as is the fact of Mobil's "domicile." To the extent dividend income is attributable to out-of-state properties and activities, this is reflected in a determination of apportionable income and the apportionment factors.

## II.

### THE VERMONT APPORTIONMENT FORMULA AS APPLIED TO MOBIL'S FEDERAL TAXABLE INCOME IS VALID UNDER THE COMMERCE CLAUSE OF THE CONSTITUTION OF THE UNITED STATES SINCE IT DOES NOT SUBJECT MOBIL TO ANY UNCONSTITUTIONAL MULTIPLE TAXATION

### A. Introductory Considerations

The unitary apportionment decisions of this Court set forth above in response to Mobil's due process of law argument and cases considered therein disposes of the substance of the commerce clause arguments of Mobil and its amicus.

In its commerce clause argument, Mobil attempts to circumvent the unequivocal and clear principles set forth in the apportionment cases of this Court on the assumption that these principles, as applied to the apportionable domestic income of domestic U.S. corporations, have no relevancy if there is included in apportionable income dividends that are received by these

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cannot be fairly considered by themselves and the whole business in the several states derives a value from the unity of use, allocation of income upon a reasonable formula is properly sustained.'" (38 Cal.2d at 228, 238 P.2d at p. 577)



corporations from their foreign subsidiaries or affiliated corporations. They center this argument on *Japan Line* (which has no relevancy here) and their argument that *Moorman* and other income tax apportionment decisions of this Court, which are controlling precedent, have no application here since such decisions involved the validity of apportionment rules which are different than specific allocation rules. (App. Br., pp. 36-37).

Before responding specifically to Mobil's abstract circuitous arguments which purportedly lead to the conclusion that only the commercial domicile possesses jurisdiction to tax so-called "foreign source income" from intangible properties, it is important to note some of the fallacious assumptions which underlie these arguments:

(1) Mobil assumes that the inclusion of its gross dividends in the Vermont apportionable income tax base, constitutes a tax on such dividends, its stock from which they are derived or its activities in regard thereto. This, of course, is no more true in regard to its dividends than it is in regard to Mobil's income from its refining and producing properties, as well as its other properties and income-producing activities, which are located entirely outside of the state of Vermont.

What Mobil fails to realize is that net taxable income is an abstract concept, resulting from a host of operational events within a time frame designated as a tax year and that the taxable incidence of an income tax is the realization of income. This point is illustrated by a comparison of *Crew Levick Co. v. Pennsylvania*, 245 U.S. 292 (1917), with *Peck & Co. v. Lowe*, 247 U.S. 165 (1918). While this court in *Crew Levick* invalidated a state gross receipt tax on receipts from goods sold in foreign commerce under the import/export clause, in *Peck* it rejected the argument that a tax on net income from export sales constituted a tax on exports. In so doing, it noted that an income tax:

> "* * * is not layed on the income from exportation because of its source * * * The tax is levied after

exportation is completed, after all expenses are paid and losses adjusted, and after the receipient of the income is free to use it as he chooses. Thus, what is taxed—the net income—is as far removed from exportation as are articles intended for export before the exportation begins." (247 U.S. at 174-175)

Furthermore, the inclusion of any item of income, such as dividend income, in apportionable income, does not constitute taxation of that income or its underlying "sources" by the taxing state. As noted in *Moorman*, the use of an apportionment formula method of computing taxable income "* * * does not purport to identify the precise geographical source of a corporation's profits * * *" (437 U.S. 267 at 273)[31]

(2) Mobil assumes that the "source" of its gross dividends in question for income tax attribution purposes is the business operations of its overseas subsidiary and affiliated corporations. Inconsistently, it also assumes that

[31]In *N.Y. Ex Rel Cohn v. Graves, supra*, 300 U.S. 308 (1936), this Court upheld the income tax of New York which was imposed on income derived from sources without New York on the basis of residence. It there stated that the question presented was:

> * * * whether there is anything in the Fourteenth Amendment which precludes the state of New York from taxing the income merely because it is derived from sources * * * located outside the State." (300 U.S. 312)

In the course of its opinion, it held:

> A tax measured by the net income of residents is an equitable method of distributing the burdens of government among those who are privileged to enjoy its benefits.
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> * * * * *
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> Neither the privilege nor the burden is affected by the character of the source from which the income is derived. For that reason income is not necessarily clothed with the tax immunity enjoyed by its source. (300 U.S. 313)
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> * * * * *
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> "The incidence of a tax on income differs from that of a tax on property." (300 U.S. 314)



this "source" of its dividend income is its "commercial domicile" in New York. It ignores the fact that a substantial "source" of this income may reasonably be attributable to its management, control and operations of a worldwide integrated petroleum and petroleum related business, including that of its foreign subsidiary and affiliated corporations, which it conducted in part in Vermont for the years in question. It further ignores (1) the fact that it is a distinct taxable entity from that of its subsidiary and affiliated corporations (*Moline Properties, Inc. v. Commissioner*, 319 U.S. 436 (1943)); and that Vermont does not purport to tax either the activities or income of Mobil's subsidiary and affiliated corporations. *In re Goodyear Tire and Rubber Co., Corporate Income Tax 1966, 1967 and 1968*, 133 Vt. 132, 335 A.2d 310 (1975).

(3) Mobil assumes that its gross dividends in question and its stock holdings in its foreign subsidiary and affiliated corporations do not constitute part of its operating properties and income, although presumably it utilizes these assets in its integrated business operations which it conducted in part in Vermont for the years in question. Without any factual foundation for it doing so, it arbitrarily excluded its gross dividends from its federal taxable income and asks this court to assume that such gross dividends (which for the year of 1972 amounted to 121% of Mobil's "federal taxable income") is not income from the operations of its trade or business, and therefore should be treated differently for constitutional purposes than its "operating income." (App. Br., footnote 23, pp. 36-37)

(4) Mobil assumes that the attribution of its gross dividends exclusively to the commercial domicile, avoids the risk of multiple taxation of the income of multistate-multinational corporations, to which the income is *exposed* by application of the *existing state income tax attribution rules*. However. there is nothing in the record to establish that, *under the existing state income tax attribution rules*, either Mobil or any members of C.O.S.T. or the N.A.M. are *in fact* exposed to any multiple taxation.

(5) Mobil assumes that diversity in apportionment and allocation rules create a risk of multiple taxation of its dividend income. Since there is no showing of any multiple taxation in fact under the present system, or that the state's present attribution rules would include in taxable income more than 100% of Mobil's income, there is no reason to conclude any risk of multiple taxation now exists or would be lessened by Mobil's "commercial domicile" argument.

(6) Mobil assumes that the risk of multiple taxation of any item of income which is included in apportionable income constitutes a risk of multiple taxation of its entire net income and that multiple risk exists if present state income tax attribution rules *plus any potential changes* would result in a multiple risk.

(7) Mobil assumes that New York, its commercial domicile, has the power to impose an income tax on all the dividend income in question. However, the record does not disclose that Mobil's stock holdings or the dividends derived therefrom are located and managed in New York. Mobil assumes that the legal fiction of "commercial domicile" alone establishes a "business situs" of the stocks and income therefrom in New York. No decision of this Court has so held in the context of any state tax.

(8) Mobil assumes that "investment" in stock of a foreign corporation and the receipt of dividends from that stock, constitutes engaging in "foreign commerce" by the owner of the stock within the preview of the commerce clause. It cites no decision in support of this novel proposition.

(9) Mobil assumes that multinational corporations have an easily ascertainable "commercial domicile" from which they conduct all of their worldwide activities, when as a matter of fact, they may have a different "commercial domicile" in reference to different aspects of their worldwide businesses. For example, in the instant case we do not know whether Mobil's foreign operations are conducted from its headquarters in New York, or elsewhere.



(10) Mobil assumes that the due process and commerce clauses alone prevent any duplicate income taxation by the states—either actual or potential. This Court has never so held.

(11) Mobil assumes that federal income tax attribution rules for federal income tax purposes control for state income tax purposes. Since federal jurisdiction is entirely different than the more limited state jurisdiction, the income tax attribution rules for federal income tax purposes cannot be applied at the state or local level since they are each grounded on distinct jurisdictional prerequisites.

From the foregoing it is evident that Mobil premises its abstract theoretical "foreign commerce" argument on a series of false premises and false assumptions which completely undermine the validity of its argument and that of its amicus. If Mobil's "foreign commerce" argument otherwise had any validity, it is obvious it has none apart from the foregoing false premises and false basic assumptions.

### B. Japan Line Ltd. v. County of Los Angeles, 47 U.S. L.W. 4477 (April 30, 1979) Refutes, Rather than Supports, Mobil's "Foreign Source" Argument Inasmuch As this Court therein Affirmed the Principle of Full Apportionment to Prevent any Unconstitutional Multiple Taxation of Domestic Corporations Engaged in Interstate Commerce.

Contrary to the argument of Mobil and its amicus, there is nothing in the holding or reasoning of this Court in *Japan Line* that supports Mobil's position that the gross dividends it received from its foreign subsidiary and affiliated corporations can be constitutionally taxed only by the state of its commercial domicile.

Inasmuch as this Court carefully limited its decision in *Japan Line* to property tax on foreign owned, controlled and registered instrumentalities of commerce

used exclusively in international commerce, there is not the slightest reason to assume that *Japan Line* supports the domicillary rule here urged by Mobil and its amicus. This is particularly true when the reasons for applying the domicillary rule in *Japan Line* are totally absent from the case at bar.

This court in *Japan Line* limited the issue there considered to:

> "* * * whether instrumentalities of commerce that are owned, based, and registered abroad and are used exclusively in international commerce, may be subjected to apportioned property taxation by a state."

It declined to rule on this question in the context of foreign owned instrumentalities engaged in interstate commerce, or domestically owned instrumentalities engaged in foreign commerce. As to domestically owned instrumentalities engaged in interstate commerce, *Japan Line* affirmed the principle of full apportionment of movable tangible properties.

Nowhere in *Japan Line* is there the slightest hint that this Court's decision there would have any application to state taxation of domestic United States corporations engaged in interstate commerce. Furthermore, it expressly affirmed, as to such corporations and as to such commerce the applicability of formulary apportionment to eliminate any undue or unconstitutional multiple burden on interstate commerce.

Mobil and its amicus curiae center their entire commerce clause arguments in this case around *Japan Line* and on the assumption that the receipt of dividend income by a domestic corporation from foreign subsidiary and affiliated corporations constitutes "foreign commerce." They have neither analyzed how they arrive at their novel "foreign commerce" conclusion, nor cited case which would characterize a United States recipient of dividends from foreign "investments" as engaged in "foreign commerce" or which would characterize the inclusion of such dividend income in the apportionable



income tax base of a state as the taxation of "foreign commerce." In the instant case, all that Vermont is attempting to tax is Mobil's corporate income reasonably attributable to its operations and activities in Vermont. The fact that there is included in the apportionable tax base the dividends in question is not a tax on "foreign commerce." Vermont is no more imposing a tax on "foreign commerce" than was New York in *Bass, Ratcliff & Gretton, supra.* This fact alone destroys Mobil's reliance on *Japan Line* and its related "foreign commerce" arguments.

### C. If a State Tax Is Fairly Apportioned to Reach Only Income Reasonably Attributable to the Taxing State, the Multiple Taxation Limitations of the Commerce Clause are Satisfied.[32]

In analyzing Mobil's "multiple risk" argument, it is significant that this court has never invalidated a properly apportioned state tax on the grounds that it exposed,

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[32]In considering the decisions of this court pertaining to the "multiple risk" argument of Mobil, it is important to place such argument in its proper context. Net income is an abstract concept. Furthermore, what constitutes "net income" for state income tax purposes, though generally geared to federal taxable income, may vary significantly from state to state. In fact, some states do not tax net income at all. Any income tax liability may be subject to special tax credits to offset other tax liabilities of the taxpayer or to special deductions. Furthermore, any otherwise identifiable item of "net income" loses any identity when it is subject to apportionment to determine "net taxable income" which is attributable to and taxed by the taxing jurisdiction.

Under these circumstances, it is inappropriate to assume that any particular item of income is specifically subject to income taxation by any state where such income represents one element of "net income" which is subject to apportionment. In this case at bar, given the nature of the apportionable net income tax base (which commingles all items of income and expenses and other deductions), after the application of the Vermont apportionment formula, it is impossible to conclude that Vermont has *in fact* taxed any of Mobil's dividends. This is particularly true where all of the income is derived from an integrated unitary trade or business carried on in part in the taxing state and only a small fraction of that income (less than 2%) is taxed by Vermont.

either interstate or foreign commerce, to the risk of multiple taxation.

In *Moorman Mfg. Co. v. Bair, supra,* this court noted that the prevention of any duplicate taxation would require uniform national rules for the division of income, *both as to apportionment and specific allocation (separate accounting) rules.* It there stated:

> "The only conceivable constitutional basis for invalidating the Iowa statute would be that the Commerce Clause prohibits any overlap in the computation of taxable income by the states. *If the Constitution were read to mandate such precision in interstate taxation, the consequences would extend far beyond this particular case. For some risk of duplicate taxation exists whenever the States in which a corporation does business do not follow identical rules for the division of income.* Accepting, appellant's view of the Constitution, therefore, would require extensive judicial law making. Its logic is not limited to a prohibition or use of a single-factor apportionment formula. The asserted constitutional flaw in that formula is that it is different from that employed by a majority of the states and that difference creates a risk of duplicative taxation. *But a host of other division of income problems create precisely the same risk and would similarly rise to constitutional proportions* * * *
>
> "A similar risk of multiple taxation is created by the diversity among the States in the attribution of 'nonbusiness' income.
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> "The prevention of duplicative taxation, therefore, would require national uniform rules for the division of income.
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> * * * * *
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> "Finally, it would be an exercise in formalism to declare appellant's income tax assessment unconstitutional based on *speculative concerns* with multiple taxation. Further, it is evident that appellant would have no basis for complaint if, instead of an income tax, Iowa had imposed a more burdensome gross receipts tax on the gross receipts from sales to Iowa customers." (Emphasis added; 437 U.S. 267 at 278-280)



In *Moorman,* in further response to alleged duplicate taxation there involved, this Court specifically found that "* * * *this record* does not establish the essential factual predicate for a claim of duplicate taxation." (437 U.S. at 276) After rejection of the assumptions on which duplicate taxation in *fact* was claimed by Moorman, this Court again reiterated that no duplicate taxation was established and that *"In any event on this record its existence is speculative."* (437 U.S. 267 at 276) In footnotes 10 and 11, this Court further noted:

> "Since Illinois did not adopt its income tax until 1970, there was no possibility of any overlap until that year. The alleged overlap in the three years following Illinois' enactment of an income tax was 34.38% in 1970, 34.51% in 1971, and 37.01% in 1972. Since there is no evidence in the record regarding the percentages of its total net income taxed in the other States in which it did business during those years, any claim that appellant was taxed on more than 100% of its total net income would also be speculative." (Ibid at 276)

If the commerce clause prohibits any risk of double taxation based on differences in the income attribution rules of the states rather than actual duplicative taxation, the *Moorman* case was wrongly decided. However, as applied to *properly apportioned state net income taxes,* potential risk has never been the constitutional standard and clearly is not the multiple risk standard in *Moorman.*

*First Federal S & L Assn. v. State Tax Commission, supra,* 437 U.S. 255 (1977) was handed down the same day as *Moorman.* One of the issues presented in *First Federal* was the risk of multiple taxation of the income of First Federal. The record below disclosed that approximately 35% of the income of the association for the years involved was derived from loans secured by real estate outside of Massachusetts (the taxing state). The appellant associations pointed out that this Court had recently in *John Hancock Mutual Life Insurance Company v. Brady,*

434 U.S. 804 (1977), dismissed the appeal of 342 So.2d 295 (1977) where the Supreme Court of Mississippi had held that Mississippi had jurisdiction to tax interest income of a foreign corporation based upon the fact that the income was derived from loans secured by recorded interests in real estate located in Mississippi. This Court disposed of this multiple risk argument by stating in a footnote

> "This argument is wholly speculative and unsupported by evidence in the record." (437 U.S. at 262)

Obviously, "evidence in the record" refers to actual, not potential, risk of duplicate taxation.

In *Northwestern States Portland Cement Co. v. Minnesota, supra,* 358 U.S. 450 (1959), this court clearly distinguished the multiple taxation question in the context of unapportioned gross receipts taxes, such as those involved in *Michigan-Wisconsin Pipeline Co. v. Calvert,* 347 U.S. 157 (1954) and *Adams Mfg. Co. v. Storen,* 304 U.S. 307 (1938) from the context of this question in apportionment cases. After referring to *Bass, Ratcliff & Gretton, Ltd. v State Tax Commission, supra,* 266 U.S. 271 (1924) and *Norfolk & W. R. Co. v. North Carolina,* 297 U.S. 618 (1936), this Court in *Portland Cement* noted:

> "These cases stem from the doctrine that *the entire net income of a corporation,* generated by interstate as well as intrastate activities, *may be fairly apportioned among the states for tax purposes* by formulas utilizing in-state aspects of interstate affairs." (358 U.S. 460)

It there then stated:

> "While the economic wisdom of state net income taxes is one of state policy not for our decision, one of the "realities" raised by the parties is the possibility *of a multiple burden* resulting from the exactions in question. *The answer is that none is shown to exist here.* This is not an unapportioned tax which by its very nature makes interstate commerce bear more than its fair share. As was said in *Central Greyhound Lines v. Mealey,* 334 U.S. 653, 661 (1948), 'it is interstate commerce which the State is seeking to reach and * * * the real question [is] whether what the State is exacting is a constitutionally fair demand by the State for that aspect of the interstate commerce to which the State bears a special relation.' *The apportioned tax is designed to meet this very requirement and 'to prevent the levying of such taxes as will discriminate against or prohibit the interstate activities or will place the interstate commerce at a disadvantage relative to local commerce.' Id.,* at 670.
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> *Logically it is impossible, when the tax is fairly apportioned, to have the same income taxed twice. In practical operation, however, apportionment formulas being what they are, the possibility of the contrary is not foreclosed, especially by levies in domiciliary States.* But that question is not before us. It was argued in *Northwest Airlines v. Minnesota,* 322 U.S. 292 (1944), that the taxation of the entire fleet of its airplanes in that State would result in multiple taxation since other States levied taxes on some proportion of the full value thereof. The Court rejected this contention as being "not now before us" even though other States actually collected property taxes for the same year from Northwest upon "some proportion" of the full value of its fleet. *Here the records are all to the contrary. There is nothing to show that multiple taxation is present. We cannot deal in abstractions.* In this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense. This they have failed to do. (Footnotes omitted; emphasis added; 358 U.S. at 462-463)



In *General Motors v. Washington,* 377 U.S. 436 (1964), this Court stated and disposed of the multiple taxation issue there involved as follows:

> "A more difficult question might arise from appellant's claim of multiple taxation. *Gwin, White & Prince, Inc. v. Henneford,* 305 U.S. 434, 440 (1939). General Motors claims that some of its products taxed by Washington are manufactured in St. Louis where a license tax, measured by sales before shipment, is levied. See *American Mfg. Co. v. St.*

*Louis*, 250 U.S. 459 (1919). It is also urged that General Motors' Oregon-based activity which concerns Washington sales might afford sufficient incidents for a similar tax by Oregon. The Court touched upon the problems of multiple taxation in *Northwest Airlines v. Minnesota, supra*, at 295, but laid it to one side as 'not now before us.' Thereafter, in *Northwestern States Portland Cement Co. v. Minnesota, supra*, at 463, we held that '[i]n this type of case the taxpayers must show that the formula places a burden upon interstate commerce in a constitutional sense.' Appellant has not done this. It has not demonstrated what definite burden, in a constitutional sense, the St. Louis tax places on the identical interstate shipments by which Washington measures its tax. Cf. *International Harvester Co. v. Evatt*, 329 U.S. 416, 421-423 (1947). *And further, it has not been shown that Oregon levies any tax on appellant's activity bearing on Washington sales.* In such cases we have refrained from passing on the question of 'multiple taxation,' e.g., *Northwestern States Portland Cement Co. v. Minnesota, supra*, and we adhere to that position." (377 U.S. 436 at 448-449)

Again, in *Standard Pressed Steel Co. v. Dept. of Revenue of Washington*, 419 U.S. 506 (1975), the Court declined to find any multiple taxation burden without an actual showing.

Notwithstanding the unequivocal holding of this Court (1) that the multiple risk standard of the commerce clause is satisfied by valid apportionment standards; and (2) that it will not engage in speculative reasoning to determine the existence of any multiple tax burden, Mobil argues that these cases simply stand for the proposition that there was no multiple risk in a constitutional sense. This argument begs the question. Since these decisions hold that, in a constitutional sense, hypothetical speculative burdens are not significant and that the commerce clause multiple burden standard is complied with by proper apportionment, Mobil's "constitutional sense" argument is a *non sequitur*.



In support of its multiple risk argument, Mobil relies heavily on the gross receipts cases (App. Br., pp. 16-18) and particularly Mr. Justice Rutledge's single opinion in *McLeod v. Dilworth Co.*, 322 U.S. 327 (1944), *General Trading Co. v. State Tax Comm.*, 322 U.S. 335 (1944) and *International Harvester Co. v. Dept. of Treasury*, 322 U.S. 340 at 349. Mobil fails to note that Mr. Justice Rutledge's remarks, which it quotes on pages 17-18 of its brief, were made in regard to unapportioned sales or use taxes. He was there talking about duplicative taxation of gross receipts by the state of origin and the state of the market of the sales. In this opinion, he definitely distinguished between risk and actual multiple burdens and also concluded that apportionment resolves any undue commerce clause burden even as to gross receipts taxes.

He there aptly noted that:

"The real danger arises most obviously when both states levy the tax." (322 U.S. 358-359)

In the course of his opinion, he further stated:

"Either one tax must fall or, what is the same thing, be required to give way to the other by allowing credit as the Iowa tax does, *or there must be apportionment.*" (Emphasis added; 322 U.S. 360)

Mobil failed to consider the following statement in the controlling decision *Harvester Co. v. Dept. of Treasury, supra:*

"Much is said, however, of double taxation, particularly with reference to the Class D sales. It is argued that appellants will in all probability be subjected to the Illinois Retailers' Occupation Tax for some of those sales, since that tax is said to be exacted from those doing a retail business in Illinois even though orders for the sales are accepted outside of Illinois and the property is transferred in another State. *But it will be time to cross that bridge when we come to it.* For example, in the *Wood Preserving Corp.* case the State to which the purchaser took the ties might also have sought to tax the transaction by

levying a use tax. But we did not withold the hand of Indiana's tax collector on that account." (Footnote omitted, emphasis added; 322 U.S. 341, 348)

In further support of its multiple risk argument, on page 19 of its brief, Mobil quotes the following statement from footnote 17 of the opinion in *Japan Line:*

> "Because California's tax in this case creates multiple taxation in fact, we have no occasion here to decide under what circumstances the mere *risk* of multiple taxation would invalidate a state tax, or whether this risk would be evaluated differently in foreign, as opposed to interstate, commerce. Compare *Moorman Mfg. Co. v. Bair,* 437 U.S. 267, 276-277 (1978), and *Washington Revenue Dept.,* 435 U.S., at 746, with, e.g., *Central R. Co.,* 370 U.S., at 615; *Ott,* 366 U.S., at 175; and *Northwest Airlines,* 322 U.S., at 326 * * *" (Slip Op., p. 18)

None of the cases in the above quoted statement remotely suggest that a validly apportioned state tax creates unconstitutional multiple taxation based on the speculative power of another state to tax.

If, as this Court has repeatedly stated, the commerce clause does not call for mathematical exactness or the rigid application of a particular formula, Mobil's multiple risk argument in the context of the validly apportioned Vermont income tax as applied to Mobil conclusively resolves Mobil's "multiple risk" argument. Mobil assumes that what constitutes apportionable income and what constitutes a reasonable apportionment formula are related to entirely different constitutional problems. If some duplicative taxation in the application of apportionment formulae is constitutionally permissible, absent congressional legislation, there is no reason why the same standard is not applicable to other income attribution rules, including specific allocation.

In any event, the controlling fact here is that this Court has never determined, as a hypothetical proposition, whether another state has jurisdiction to tax, irrespective of what risk standard is required by the commerce clause.



It has consistently refused to engage in any speculative reasoning or analysis of either the commerce clause or a taxpayer's exposure to multiple taxation in deciding the commerce clause question before it. What Mobil is asking this Court to do in this case is to speculate as to whether or not, under the circumstances of this case, New York is entitled to attribute to itself, based on the legal fiction of commercial domicile, almost all of Mobil's entire net income for the years in question. Resolution of this question, within the framework of judicial proceedings, is proper only if and when New York seeks to exercise such jurisdiction and its power to do so is appropriately challenged by a taxpayer. This is particularly true when this Court has never before considered this constitutional issue, that is, the right of the "commercial domicile," solely on the basis of the legal fiction "commercial domicile," to tax the entire income from intangibles derived by the taxpayer from its unitary business operations. It should do so only in the context of an actual case or controversy.

In this connection, we are confident that if New York attempted to exercise such jurisdiction, Mobil would advance various factual and legal propositions to indicate that the legal fiction of commercial domicile should not be so applied to it.

In further regard to Mobil's multiple risk argument, it is significant to examine how it arrives at its conclusion that it is exposed to a risk of multiple taxation. The reasoning of Mobil in support of its "multiple risk" commerce clause argument is based on a mixture of fact and fantasy. Mobil argues that the *fact* that it is not subject to multiple taxation is not significant in a constitutional sense. It claims that any risk of multiple taxation must consider any *potential changes* in the *existing* attribution rules and thus, since New York could change its attribution rules to tax dividends in full based on "domicile," there is a potential risk of multiple taxation. Thus, Mobil argues that if a *combination of existing attribution rules plus any potential changes in the existing rules* could result in a risk of multiple

taxation, this triggers invalidity of any apportionment rule under the commerce clause. In other words, unconstitutional risk of multiple taxation exists if the presently employed attribution rules *plus* any *potential* changes exposes dividends to a *risk* of multiple taxation. Under such a constitutional standard, even if all of the states employed identical attribution rules to dividend income, these rules would not pass constitutional muster *if* any state could constitutionally change its rules to attribute more dividend income to it than under its existing uniform rule.

In any event, irrespective of whether prior decisions of this Court, as an abstract proposition, have adhered to the risk versus actual multiple burden test in analyzing commerce clause questions, there can be no argument with the proposition that this Court has uniformly found that a reasonably apportioned net income tax places no prohibitive burden upon interstate commerce in a constitutional sense. As noted in *Moorman*, this is equally true in regard to uniform allocation rules as it is in regard to uniform apportionment rules. In short, this Court has left any such considerations to the political processes of the respective states and the Congress. Thus, the multiple risk argument of Mobil and its amicus is without merit within the context of this case.

### D. In Conformity with the Dual Purposes of the Commerce Clause to Require Interstate Commerce to Pay Its Way and to Prevent Discriminatory Taxation of Interstate and Foreign Commerce, the Commerce Clause Has Been Properly Interpreted by this Court to Preclude Only Undue Multiple State Taxation in Fact.

Mobil is here contending for what amounts to an exemption of substantially all of its net income from state income taxes based on its "multiple risk" argument. It argues that this result is justified because its claimed income tax immunity is attributable solely to New York's



policy in not exercising its power to tax dividends based on the legal fiction of "commercial domicile." Assuming that this is so, the question remains as to whether the purpose of the commerce clause is better served by interpreting it to conform with the claimed exemption of Mobil rather than in support of the legitimate power of Vermont to include Mobil's dividends in apportionable income. Clearly, Vermont must do so if it can effectively impose its corporate income tax commensurate with the benefits it has afforded Mobil relative to the income producing activities conducted by Mobil in Vermont. Also, Vermont must do so if it is to apply its corporate income tax in a manner that does not subject Mobil's instate competitors to discriminatory taxation.

This Court has repeatedly held that the commerce clause is not to be interpreted to grant interstate businesses a tax-free ride. As stated by this Court in *General Motors Corp. v. Washington*, 377 U.S. 436 (1964):

> "We start with the proposition that '[i]t was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business.' *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938). 'Even interstate business must pay its way,' *Postal Telegraph-Cable Co. v. Richmond*, 249 U.S. 252, 259 (1919), as is evidenced by numerous opinions of this Court. (377 U.S. at 439)
>
> * * * * *
>
> "A careful analysis of the cases in this field teaches that the validity of the tax rests upon whether the State is exacting a constitutionally fair demand for that aspect of interstate commerce to which it bears a special relation." (377 U.S. 440)

Likewise, this Court has repeatedly held that the commerce clause was designed to protect commerce from discriminatory tax burdens. As stated in *Northwestern States Portland Cement Co. v. Minnesota, supra*, 358 U.S. 450 (1959):

> "Nor may a State impose a tax which disciminates against interstate commerce either by providing a direct commercial advantage to local business (cases cited) or by subjecting interstate commerce to the burden of 'multiple taxation' (cases cited)." (358 U.S. 458)

These dual constitutional requirements can best be implemented by this Court in construing the commerce clause to prevent any undue burdens on commerce as a matter of fact. In the instant case, if there is no undue burden imposed on Mobil as a *matter of fact*, should this Court nevertheless conclude that it exists *as a matter of constitutional law* by speculating on the power of New York to tax the dividends of Mobil in full by application of the legal fiction "commercial domicile"? When the competing demands of the states and the commerce clause are weighed in the balance, there is no reason why an undue burden *in fact* should not constitute the constitutional standard. Until this occurs, interstate commerce is not disadvantaged taxwise by the states.

This interpretation of the commerce clause is supported by practical considerations. It would avoid the unreasonable consequence—almost complete state income tax immunity—which Mobil and its amicus seek in this case, based on abstract constitutional and factual considerations. It eliminates any constitutional guessing pertaining to the hypothetical and speculative taxing powers of other states or countries in relation to the facts and circumstances of any particular taxpayer. It represents a construction of the commerce clause in conformity with business, economic and political reality. It places constitutional substance over constitutional form. It also enables this Court to interpret commerce clause limitations on state taxing powers within the context of actual controversies between the states and taxpayers directly affected by such decisions.

In arguing what it characterizes as "the propriety of the risk test" (App. Br., pp. 22-23), Mobil concludes:



> "We submit that the potential for multiple taxation, rather than the actuality of multiple tax burdens, is the proper test of the constitutionality of state taxes under the commerce clause." (App. Br., p. 23)

What Mobil fails to note is that the *potential* for multiple taxation under the facts and circumstances of this case is only speculative. It does not urge that there is the slightest possibility that New York will tax its dividends on the basis of the fiction of "domicile." In fact, Mobil and its amicus curiae urge this Court to accept this fiction, not to prevent potential multiple taxation, but to prevent any taxation by the states of what amounts to in many instances to all or substantially all of their net income. Thus, Mobil and its amicus curiae are asking this Court to interpret the commerce clause to preclude any *theoretical constitutional risk* of multiple taxation based on an alleged comparison of the *existing attribution rules* plus *any potential changes* in such rules. Furthermore, this Court has already decided any policy issue pertaining to multiple risk under the commerce clause that could possibly be involved in this case.[33]

While Mobil has limited its argument in this case to so-called dividends from "foreign sources," it is readily apparent that its argument and that of its amicus, in principle, cuts to every aspect of what constitutes the taxable income of multinational corporations for state income tax purposes. Here, Mobil is asking this Court to constitutionally mandate an exclusion from federal taxable income for Vermont income tax apportionment purposes. If this Court is empowered under the commerce clause to determine the appropriate attribution rule for any class of income, there is no reason to suppose that it is

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[33]As indicated *supra*, at pages 55-61, Mobil and its amicus curiae completely ignore the fact that under repeated decisions of this Court fairly apportioned net income taxes have been held to comply with the multiple taxation requirements of the commerce clause. Therefore, Mobil's potential versus actual multiple tax burden argument, has absolutely no significance here.

not also empowered to do so for any other class of income. This is particularly true in regard to income from all forms of intangible properties.

The type of problems this Court would be enmeshed in unless it held that the constitution requires full apportionment of all unitary income of a unitary trade or business is set forth on pages 197-224 of Volume 1 of the "Willis Report."[34]

For example, as indicated therein on pages 204-205, interest attribution rules pertaining to interest income may involve apportionment or allocation. Allocation rules applicable to interest income may include the legal domicile, commercial domicile, principal place of business, business situs of the interest-bearing asset, location of the payor of the interest or on the basis of actual situs of the asset, as well as various combinations of the foregoing. In regard to dividends, the Willis Report at page 206 of Volume 1 notes that with only a few exceptions "the rules governing the specific allocation of dividends are the same as the rules for the allocation of interest income."

Furthermore, if uniform attribution rules is required concerning assigning of income under the commerce clause, there is also involved, as indicated by the Willis Report (Ibid., pp. 220-224), special problems pertaining to offsetting expenses. For example, in the instant case, if this Court should conclude that Vermont lacks the power to include in apportionable income the dividends in question, is Vermont entitled to offset interest and various overhead, management, research and other expenses resulting from activities concerning the operations of its foreign subsidiary and affiliated corporations, etc.? If so, in accordance with what standards or criteria? These considerations led the Willis Committee to recommend full apportionment of the entire net income of corporations. They have likewise led the states in the same direction so that now the states all generally require the apportionment of all business income.

[34]State Taxation of Interstate Commerce, Report of Special Subcommittee on State Taxation of Interstate Commerce of the Committee on the Judiciary House of Representatives, Vol. 1 (H.R. 1480, 88th Cong. 1964)



However, "net taxable income" and apportionment and allocation rules applied to "net income" are not necessarily uniform and any rigid constitutional requirement, such as specific allocation of dividend income to the commercial domicile, has a ripplying effect. It creates a whole new series of income tax base and attribution problems. For example, if Vermont and other states cannot include "dividends" in apportionable income but can include all "operating income," this immediately raises a whole series of problems in determining what truly constitutes "dividend income" versus "operating income" for constitutional purposes. The fact that Mobil's dividends are labeled by it as income from "investments" in stock rather than from its worldwide unitary business operations should not control for constitutional purposes. Furthermore, specific allocation of dividends would augment the need for the states to resort to worldwide "combined reporting" or alternatively to attempt by "separate accounting" to unravel complex interrelated transactions pertaining to a unitary trade or business conducted by a U.S. parent and its foreign subsidiary and affiliated corporations which involve the difficult and vexing problems associated with section 482 adjustments under the Internal Revenue Code.[35]

[35]For a discussion of Section 482 problems and alternative approaches, such as "combined reporting" see the Note, Ibid., footnote 25, p. 20.

The type of income attribution problems associated with United States domestic parent corporations in their dealings with their foreign subsidiary and affiliated corporations is illustrated by the California Board of Equalization *Appeal of Texaco, Inc.*, decided January 11, 1978 discussed *supra* in footnote 25. The nature of these problems is also illustrated by an example involving Delaware and Getty Oil. As reported in *Tax Notes*, Sept. 1 and October 20, 1975, for several years in the 1970's Getty did not report any taxable income to Delaware, where it has substantial properties, payroll and investments. Getty

Thus, while Mobil and its amicus purport to deal with a very narrow issue in this case in an abstract manner, this case involves many more ramifications than the constitutionality of an apportionment formula. This Court was aware of this fact in *Moorman*. It noted that *Moorman* posed, in substance, a whole spectrum of income base and attribution problems in addition to the narrow question of the validity of a particular apportionment formula. It therefore left resolution of this, *as well as necessarily related attribution and base questions* to the political arena for resolution.

We thus fail to see any merit in the argument of Mobil and its amicus that the multiple risk standard should be applied in the instant case to invalidate Vermont's reasonable apportionment of Mobil's income to its Vermont activities.

### E. There is No Merit to Mobil and its Amicus Curiae's Argument that So-Called "Risks of Multiple Taxation" of Dividend Income is Reduced by Substituting the "Commercial Domicile Fiction" in Place of the Existing Income Attribution Rules.

On pages 23-37 of its brief, Mobil sets forth various abstract arguments pertaining to what it captions as the risks of multiple taxation of dividends from foreign commerce. This argument is premised on the unsupportable proposition that Vermont, in including Mobil's dividends from its foreign subsidiary and affiliated corporations in apportionable income, is somehow imposing its income tax on "foreign commerce" in contravention of this Court's decision in *Japan Line*. However, as heretofore indicated on pages 53-55 *supra*, *Japan Line* has no application to division of income attribution rules

apparently achieved this remarkable result through its transfer pricing arrangements with its subsidiaries and affiliates. Any such tax consequences are compounded here if the argument of Mobil and its amicus are controlling.



pertaining to interstate commerce of domestic United States corporations since Vermont is not taxing Mobil's "foreign commerce."

Assuming arguendo that Vermont is taxing "foreign commerce," still, there is no showing by Mobil that its income in question is subject to any potential multiple taxation under the existing state income tax attribution rules. By an abstract theoretical analysis, Mobil attempts to demonstrate that differences in apportionment rules of the states result in duplicate taxation (App. Br., pp. 27-28, footnote 12). Although Mobil asserts that "the potential for double taxation by the twenty-seven states — in all of which Mobil, like many other multinational corporations do business — is manifest from the diversity in the formulas employed by those states" (App. Br., p. 27) Mobil fails to indicate, *as to it* why this is so. Nor is there any information concerning the impact of such diversity on the "many other multinational corporations" which are allegedly similarly situated to Mobil.

In substance, then, without any proof whatsoever, Mobil and its amicus curiae ask this Court to accept as a fact, in interpreting commerce clause limitations on state taxing powers, that diversity in state apportionment rules and potential for double taxation are one and the same. Nothing could be further from the truth. As indicated in Jerome R. Hellerstein's article, *"State Taxation Under the Commerce Clause: An Historical Perspective,"* 29 Vand. L. Rev. 335, 347 (1976):

> "Diversity in state or local apportionment, which often results in undertaxation of an enterprize, is * * * unfair to the governments and oppressive to competitive intrastate business."

The validity of this statement can be demonstrated by a cursory examination of those differences relied upon by Mobil in footnote 12 on page 27-28 of its brief to "prove" a risk of multiple taxation under existing apportionment rules. There, Mobil first relies on the fact that in some states the taxpayer has the option to use either UDITPA

or the "traditional formula." The fact that a taxpayer has this option is a difference that can only lessen, not augment, a taxpayer's risk of multiple taxation.

Next, Mobil relies upon the variation and the weight given the apportionment factors employed by the states and some variations among the states in implementation of the same factors. While Mobil points to differences in the sales and property factors, there is no indication as to whether these differences result in a substantial gap rather than overlap in the attribution of apportionable income. It is further obvious that any potential risk of multiple taxation of dividends under the present system would have to take into consideration what dividends are actually subject to tax by the states. This we do not know from Mobil's analysis.

Appendix F attached to Mobil's brief (App. Br., p. 37a-39A) lists "only jurisdictions which include foreign source dividends, in part or in whole, in the tax base." The table refers to an undisclosed item captioned, "All Taxable Dividends." We do not know to what extent and on what basis dividends are taxable by any state. The table is otherwise unreliable.

California Montana, Idaho, Kansas, Oregon and Colorado employ worldwide combined reporting which eliminates the intercorporate dividends of the combined corporations which conduct an integrated unitary business. This presumably would include all the dividends in question. Furthermore, California has adopted UDITPA which requires the apportionment of dividends to the extent they constitute "business income" as defined therein, the applicability of which, due to California precedent, is currently in litigation in California. The *Times Mirror Company v. Franchise Tax Bd.*, Los Angeles Superior Court No. C1723731; *In the Matter of the Appeal of Standard Oil Company of California*, Calif. Bd. of Equal.

Also, the table erroneously indicates that Arizona, Louisiana, Minnesota, Mississippi, Oklahoma and South



Carolina, in addition to California, allocate all taxable dividends to the commercial domicile of the payee corporation.

Louisiana law provides for the specific allocation of dividends and profits from sales or exchanges of intangible property to the state in which the securities or credits producing such income "shall have their business situs." If they have not acquired a business situs, income from such properties of a corporation are then allocated to the commercial domicile. The Louisiana law further provides that dividend income from controlled corporations (50% or more of voting stock) having a situs in Louisiana "shall be allocated to the state or states in which is earned the income from which the dividends are paid * * *" (La. Rev. Stat. Ann. § 243, P.H. State Income Tax Reporter, Louisiana ¶ 12,644)

Minnesota law requires the apportionment of income from intangible properties where the property is employed in a unitary business carried on partly within and without Minnesota. (Minn. Stat. § 290.17, P.H. State Income Tax Reporter, Minnesota ¶ 94-06 & ¶ 94-067a). Even where the income was not associated with the unitary business, the Supreme Court of Minnesota held that dividends could not be taxed by Minnesota by application of the legal fiction of "commercial domicile" since it interpreted prior decisions of this Court to permit taxation of intangibles by the "commercial domicile" only if they acquire a "business situs" at the commercial domicile. *Marshall-Wells Co. v. Commissioner of Taxation*, 220 Minn. 458, 20 N.W.2d 92 (1945).[36]

[36]The foregoing references to Minnesota law are consistent with its decisions in *Montgomery Ward & Co. v. Commissioner of Taxation*, 276 Minn. 479, 151 N.W.2d 294 (1967) and *Great Lakes Pipeline Co. v. Commissioner of Taxation*, 272 Minn. 403, 138 N.W.2d 612 (1965) wherein it applied the unitary concept to determine what constituted apportionable interest income.

Mississippi law likewise provides for the apportionment of all business income, including that from intangible properties, if specific allocation or "separate accounting" is found impossible because of the unitary nature of the taxpayer's instate and out-of-state business operations (Miss. law, § 27-7-23 as amended by Ch. 475, Laws of 1978; P.H. State Income Tax Reporter, Mississippi § 92-532). Mississippi Reg. 1.27-7-23(7) provides for apportionment of federal taxable income, including interest income and dividends from a unitary trade or business.

Oklahoma law in turn provides only for the specific allocation of income from intangibles "which is not a part of business carried on within and without the state of a unitary character." Intangible income of a non-unitary character is allocated to the business or commercial situs or if there is no such situs, apart from the commercial domicile, then to the "commercial domicile." (Okla. Stat. Tit. 68, § 2358A; P.H. State Income Tax Reporter, Oklahoma ¶ 12, 711)

Arizona law specifically states that "Income from business carried on partly within and partly without this state shall be apportioned in such a manner as is fairly calculated to apportion such income among the states or countries in which such business is conducted." It contains no specific provision allocating income from dividends to the commercial domicile and provides for offsetting any interest expense if interest or dividend income is specifically allocated. (Ariz. Rev. Stat. § 43-135(g); P.H. State Income Tax Reporter, ¶ 12, 738.22) The income tax regulations of Arizona specifically provide for full apportionment of income from a unitary trade or business. Only income not connected with the unitary business is subject to allocation (Regulation § 135-8(b); P.H. State Income Tax Reporter, Ariz. ¶ 11,289.55)

North Carolina law employs the UDITPA definition of "business income" and "nonbusiness income" (N.C. Gen. Stat. § 105-130.4(1) and (5)) and provides for the specific allocation of dividend and other income from



intangibles only to the extent such income is "nonbusiness income." It further provides for apportionment of all business income of corporations (except public utilities and some excluded corporations) by the general three-factor UDITPA apportionment formula (N.C. Gen. Stat. § 105-130.4(i)). Nonbusiness dividends from a corporation in which the payee corporation owns 50% of the payor corporation is allocated to the state if the payor corporation is subject to tax in the state based on that portion of the payor corporation's income taxable in the state (N.C. Gen. Stat. § 150-130.4(f)). The North Carolina statutory pattern, following the unitary concept, accords with the holding in *Maxwell v. Kent-Coffey Mfg. Co.*, 204 N.C. 365, 168 S.E. 397 (1933), aff'd 291 U.S. 642 (1934).

Thus, Mobil has failed to substantiate its argument and that of its amicus that the present state income tax treatment of so-called "foreign source dividends" result in *any risk or potential multiple taxation of such dividends* — assuming the correctness of the basic assumptions on which such an argument is structured. In fact, an examination of the present state income tax system overwhelmingly supports the proposition that no state relies *solely* on the legal fiction of "commercial domicile" for the attribution of dividend income or other income from intangibles. To the contrary, there appears to be an almost unanimous consensus among the states that all unitary income of a unitary trade or business should be divided by reasonable apportionment rules.

**F. There is No Valid Political, Economic or Business, or Precedental Validity to the Argument of Mobil and its Amicus Curiae that the Commerce Clause of the United States Should be Interpreted to Permit Only the State of the Taxpayer's "Commercial Domicile" to Tax Dividends or Any Other Intangible Properties Under the Facts and Circumstances of this Case.**

On pages 29-37 of Mobil's brief, it seeks to justify the broad tax immunity that it and its amicus curiae seek in this case under the following headings of its brief:

1. History and the Judicial Decisions Support Taxation of Dividends Only by the State of Commercial Domicile. (App. Br., pp. 29-30)

2. Fiscal Policy Considerations Underlying Jurisdiction to Tax Justify Taxation of Dividends Solely by the State of Commercial Domicile. (App. Br., pp. 30-34)

3. Commerce Clause Decisions of this Court Support Limitation of the Taxation of Foreign Source Dividends to a Single State to Avoid Multiple Taxation. (App. Br., pp. 34-36)

4. Affirmation of the Sole Power of the State of Commercial Domicile to Tax Foreign Source Dividends is not Inconsistent With the *Moorman* Case. (App. Br., pp. 36-37)

We will here respond to this argument of Mobil by first considering the *Moorman* case; secondly, policy considerations involved in limiting state income tax jurisdiction to the commercial domicile; thirdly, the history and judicial decisions pertaining to taxation of dividends; and lastly, Mobil's argument that decisions of this Court support its exclusive "commercial domicile" jurisdictional argument.

### 1. Moorman and Cases of Like Import Control the Disposition of this Case Inasmuch as There is Here Involved Only the Question of the Constitutionality of the Reasonable Income Tax Attribution Rules of the Vermont Corporate Income Tax as Applied to the Unitary Income of a Unitary Business Conducted in Part in the State of Vermont.

The issue before this court in *Moorman* was the constitutionality of the Iowa single-sales-factor income tax apportionment formula within the purview of the commerce and due process clauses of the United States



Constitution. The taxpayer there (Moorman Mfg. Co.) was engaged in interstate commerce and sold products in Iowa which it manufactured in Illinois. Moorman paid income tax to Iowa on its net income attributable to Iowa by the sales factor apportionment formula and Iowa's specific allocation rules.

Significant to this case, this court rejected the arguments of Moorman that an apportionment formula imposed an income tax on any specific "income" sources or transactions. As discussed *supra* at pages 56-57, it further rejected the argument that it was its function, under the commerce clause, to prescribe uniform national rules for the attribution of an income tax base among the respective states. In discussing its role under the commerce clause, it did not differentiate between those states attribution rules which are embodied in apportionment formulas and those rules which are embodied in other division of income rules, such as "separate accounting" and "specific allocation." In fact, it was keenly aware of the interrelationship and interdependence of all state income tax attribution rules and for that reason did not isolate its consideration of the validity of the Iowa apportionment formula apart from other attribution rules. It noted a potential inconsistency if it were to deny Iowa the constitutional authority to apportion income by a sales distination factor formula and permit another state, within constitutional limitations, to impose a gross receipts privilege tax on all instate receipts connected with instate activities.

In contending that *Moorman* is not controlling here as to whether or not this Court should interpret the commerce clause to require specific allocation (separate accounting) of dividends to the "commercial domicile" for state income tax division of income purposes, Mobil and its amicus completely ignore the true significance of the *Moorman* decision. In addition, they completely ignore the fact that this case, like *Moorman*, specifically involves the validity of an apportionment formula. Mobil is asking this Court here to declare an apportionment formula unconsti-

tutional for reasons not distinguishable from those advanced by Moorman in the *Moorman* case.

While Mobil states in its brief that:

> A compelling factor in *Moorman* was this Court's "unwillingness to strike down the Iowa apportionment formula was that the prevention of duplicate taxation would require national uniform rules for the division of income (437 U.S., at 279; App. Br., p. 32),"

it necessarily concludes that the assignment of income to the commercial domicile would not constitute a judicially prescribed national uniform rule for the division of income. This argument is absurd on its face! If attributing income from intangible properties solely to the commercial domicile, for state income tax purposes, is not a uniform national rule for the division of income, then nothing is!

Thus, *Moorman*, contrary to Mobil's argument and the argument of its amicus, is controlling precedent here since this Court in *Moorman*, in refusing to invalidate Iowa's single-sales-factor on the ground that it was not its function to prescribe uniform national rules for the division of income for state income tax purposes, necessarily decided that it would not prescribe a uniform national rule for the specific allocation of income.[37]

2. **Fiscal Policy Considerations, as Well as History, do Not Support Exclusive Taxation of Dividend Income and Other Intangibles for State Income Tax Purposes by the Commercial Domicile But Rather Supports Apportionment of Dividends and Other Intangibles to the Extent that Such Intangible Properties and the Income Derived Therefrom Constitute Integral Parts of the Integrated, Unitary Business of the Taxpayer Which is Conducted in Part in the Taxing State.**

[37]Furthermore, there is no basis for construing the commerce clause any differently in the context of the prescription by this Court of uniform apportionment rules than in the context of its prescription of uniform allocation rules. All state income tax attribution rules are necessarily intertwined. For constitutional purposes, they are not distinguishable. This fact was specifically noted and discussed by this Court in *Moorman*. What Mobil and its amicus ask this Court to do here is what it specifically refused to do in Moorman, that is mandate a uniform constitutional rule for the division of income.



Mobil, in arguing that fiscal policy considerations underlying jurisdiction to tax justify taxation of dividends solely by the state of "commercial domicile," premises this argument on the property tax situs domicillary rule enunciated by this Court in *Wheeling Steel Corp. v. Fox*, 298 U.S. 193 (1936) and *First Bank Stock Corp. v. Minnesota*, 301 U.S. 234 (1937). It also bases this argument on its due process argument that its "investments" in stocks of its subsidiary and affiliated corporations were unrelated to its worldwide petroleum and petroleum related business which it conducted in Vermont and in every other state in the United States and the District of Columbia.

It further predicates this argument on the assumption that it obtained this dividend income from its "business and activities as a holding and investment company" which are not connected with its Vermont activities. In regard to this unsubstantiated assertion, the record is entirely silent as to what "holding and investment company" activities were conducted by Mobil in New York or elsewhere to justify their taxation in full by what Mobil proffered in the record in this cause as its "commercial domicile." In fact, there is no claim in the record in this cause that *any activity of Mobil concerning any of its dividends in fact took place in New York*. Thus, it is not known what activities Mobil conducted or where it conducted those activities to which it would attribute the great bulk of its federal taxable income for the years in question. Furthermore, as indicated in Exhibit 8 (A75-A78) and table, *supra*, p. 23, substantially all of Mobil's dividends in question were derived from three wholly-owned subsidiary corporations and Mobil's 10% interest in ARAMCO. Yet, the record is barren as to the nature of their business activities and Mobil's activities in regard

thereto. Thus, on the basis of undisclosed and mythical facts pertaining to Mobil's "investment" activities [which were fully expensed and apportioned, including any sales or services of Mobil connected with its subsidiaries and affiliated corporations and their subsidiaries and affiliates, for Vermont income tax purposes], this Court is asked in substance to attribute all intangible income exclusively to the legal fiction of "commercial domicile" as a reasonable interpretation and application of the commerce clause restrictions on state taxing power.[38]

*Wheeling Steel Corp. v. Fox, supra,* constituted a landmark decision in upholding the power of the state of the "commercial domicile" to subject intangible properties to unapportioned property taxation. It upheld West Virginia's power to tax the intangibles there involved (bank deposits and accounts receivable) on the basis of the "commercial domicile" rule only after an extensive

[38]In advancing this argument, Mobil in footnote 19 on page 32 of its brief, attempts to sidestep the legal domicile's jurisdiction to tax because its commercial and legal domicile are both in New York. It purports to also sidestep the "business situs" issue by asserting that "the business situs question, however, does not arise in the case at bar, since Mobil's stocks in the foreign corporations whose dividends are at issue in this case had no business situs in Vermont." (App. Br., footnote 19) Mobil, in footnote 19, recognizes that "if intangibles have become an integral part of a business carried on in a state, they acquire a 'business situs' and may be taxed in that state." In so arguing, it assumes that "business situs" for income attribution rules within the context of an apportionment formula is limited to specific allocation property tax situs rules. Mobil fails to note (1) that all of the decisions of this Court which have applied apportionment principles have uniformly upheld the inclusion in the apportionable tax base of all the properties, values or income attributable to the unitary business carried on in part in the taxing state and (2) that they have uniformly placed the burden on the taxpayer to show that any apportionment formula reaches values, properties or income not reasonably attributable to the taxing state. This is nothing more nor less than applying the "business situs" rule in the "unitary rule" context.

While Mobil here presumes to present a new and novel question to this Court, it ignores a path that this Court has been down innumerable times in deciding utility property tax cases, net worth franchise cases and corporate income tax cases by application of unitary principles.



examination of facts to show that such intangibles were integrated with Wheeling Steel's business at its commercial domicile in West Virginia.

In response to the argument that the intangibles in question ought to be attributable in part to Ohio where the manufacturing operations attributable to the creation of the intangibles were carried on, this Court was careful in *Wheeling* to distinguish the property tax there involved from a net income tax. It there stated:

> "In the face of these facts, it cannot properly be said that the credits arise either where the goods are manufactured or at the sales offices where the orders are taken. The tax is not on the manufacturing or on the privilege of maintaining sales offices. *The tax is not on the net profits of a unitary enterprise demanding a method, not intrinsically arbitrary, of making an apportionment among different jurisdictions with respect to the processes by which the profits are earned. Underwood Typewriter Co. v. Chamberlain,* 254 U.S. 113, 120, 121; *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n,* 266 U.S. 271, 282, 283; *Hans Rees' Sons v. North Carolina, supra.* Such a tax on net gains is distinct from an *ad valorem* property tax on the various items of property owned by the Corporation and laid according to the location of the property within the respective tax jurisdictions. Here, the tax is a property tax on the accounts receivable, as separate items of property, and these are not to be regarded as parts of the manufacturing plants where the goods sold are produced. (Emphasis added; 298 U.S. at 212)

The inference to be drawn from the above-quoted statement of this Court in *Wheeling Steel* is that if *Wheeling* had involved an income tax and thus what was taxed was the profits of the business activities giving rise to the accounts receivable and bank deposits, a rule of apportionment would have been proper.

Again, within a property tax context, this Court in *First Bank Stock Corp. v. Minnesota,* 301 U.S. 234 (1936) applied the business situs rule to shares of corporate stock:

"* * * which, because of the *use in a business* of the owner, may be treated as localized, for purposes of taxation *at the place of the business* * * *" (Emphasis added; 301 U.S. 238)

This Court there aptly stated:

"The rule that property is subject to taxation at its situs, within the territorial jurisdiction of the taxing state, readily understood and applied with respect to tangibles, is in itself meaningless when applied to intangibles which, since they are without physical characteristics, can have no location in space. See *Wheeling Steel Corp. v. Fox, supra,* 209. The resort to a fiction by the attribution of a tax situs to an intangible is only a means of symbolizing, without fully revealing, those considerations which are persuasive grounds for deciding that a particular place is appropriate for the imposition of the tax." (301 U.S. 240-241)

Thus, if this Court should conclude, as urged by Mobil and its amicus, that foreign commerce dictates this Court to make a choice between including the dividends in question and other intangibles from so-called foreign sources in apportionable income versus their taxation solely at the "commercial domicile," policy considerations, under the facts and circumstances of this case, are clearly defined. The question is whether or not the legal fiction of "commercial domicile" should control or whether the unitary concept embodied in all the apportionment decisions of this Court and various state courts should control taxation of income from intangibles.

The underlying basic considerations involved in a determination of where the income from dividends from subsidiary and affiliated corporations of large complex multinational corporations such as Mobil and the members of C.O.S.T. should be attributed for state income tax purposes is considered in "Taxation of Income from Intangibles of Multistate-Multinational Corporations," 29 Vand. L. Rev. 401 (1976). In there discussing the attribution of dividend income to the commercial domicile of the payee corporation, it is stated:

* * * * *



"In considering the assignment of income on the basis of commercial domicile, four important factors should be considered. First, for a state constitutionally to tax 'intangible' income, case law indicates that the intangible property must have benefited from or been protected by the laws of the 'commercial domicile.' This requires a tie-in of activities at the commercial domicile with the intangible investments. If no activity is carried on at the commercial domicile in regard to the intangible investments and if these investments are not related to the commercial domicile activities of the corporation, there would appear to be no constitutional justification for taxation of the intangibles or income from them by the commercial domiciliary state. Secondly, the facts that support taxation at the commercial domicile by reference to the utilization of the intangibles in the overall business of the payee corporation (unitary concept) also support taxation of the intangibles or income derived from them by the 'business situs' states. Thirdly, to assign passive intangible investments to the state where minimal activities concerning the investments take place would be unrealistic. In the case of investments of a parent corporation in controlled affiliated corporations, it is more logical to assign the income on the basis of the location of the parent corporation's activities associated with the business operations of the affiliated corporations. Fourthly, if no one state can legitimately claim a right to tax intangible income to the exclusion of other states, apportionment of intangibles and income from intangibles on the basis of the overall activities of the payee corporation, if not constitutionally required, is the only fair and equitable way of assigning intangible income. This supports full accountability without duplicate taxation, and lends substance to the benefit and protection doctrine by assignment of income to those states that confer benefits and protection to the corporate taxpayers.

* * * * *

"More importantly, since the commercial domicile activities are closely associated with a unitary corporation's business activities everywhere, facts that support taxation of income from passive

investments in intangibles at the commercial domicile also support taxation on an apportionment basis by the states in which the corporation carries on its business activities. It is incongruous to assign income solely to the commercial domicile predicated on the assumption that the corporation's activities in the commercial domicile further the overall corporate business wherever it is conducted and thus, to disregard the claims of the other states where the corporation carries on its business." (29 Vand. L. Rev., pp. 413-414; footnotes omitted)

In discussing the question of whether income from intangibles should be attributed to the states in which the payee corporation carries on its business activities, this article further reads:

"When a corporation acquires, manages, and disposes of intangible property to produce income in the regular course of the corporation's trade or business, that income should be attributable among all the states in which that trade or business is conducted. In substance, this assigns intangible income to the 'business situs' on the basis of benefits and protection afforded as a result of the activities of the corporation. Business situs concepts also form the basis of assigning intangible income to the commercial domicile of a corporation. Certainly this business situs concept offers an alternative that is preferable to the assignment of intangible income on the basis of the legal fictions of commercial or legal domicile or on the basis of the activities of the payor corporation.

"The more difficult question involves the assignment of income from intangible property that represents passive investments of the corporation. If these passive investments have been made possible by the business activities of the corporation in the states in which those business activities have been conducted, and if the income from these passive investments is used generally by the corporation in carrying on its trade or business, should not income from these investments be attributable to the states in which the corporation carries on its business activities?

* * * * *



"Whether the corporate activity test is best depends upon the reason for resorting to an apportionment method of assigning income in the first instance. Income of multistate and multinational businesses is apportioned because it is not possible to allocate the income accurately to the sources or to the activities that these businesses carry on in each taxing jurisdiction. The purpose of apportionment is to divide the entire income tax base of a corporation among those states that have an otherwise indeterminate but legitimate claim to a portion of that tax base.

* * * * *

"* * * the underlying jurisdictional basis for taxation at the commercial domicile, apart from arbitrary property situs concepts, is the notion that the intangibles are business assets, and income from intangibles is income attributable to the business.

* * * * *

"When more than one state taxing jurisdiction has a legitimate claim to the right to tax income from passive investments in intangibles based on the activities of the payee corporation, the assignments of such income by an apportionment formula produces the most equitable result. Indeed, it may be constitutionally required unless the intangible investments are not integrally related to the corporation's business activities. Even if the intangibles are not utilized by a corporation in the conduct of its business, assignment of the income to the 'commercial domicile' is constitutionally suspect. Even when investments in intangibles require corporate activity, the most reasonable rule is to assign the resulting income to the states in which the overall corporate activity is conducted. Otherwise, the income would be assigned on the basis of a meaningless fiction, with the result that large segments of corporate income would be totally exempt, 'nowhere income.'" (29 Vand. L. Rev., pp. 414-419; footnotes omitted)

Assuming arguendo that the legal fiction of "commercial domicile" is superior to the unitary apportionment method for the division of income from passive "investments" in intangible properties, the question here is

whether the choice of methods should be a function of this Court. In regard thereto, Jerome R. Hellerstein in "State Taxation Under the Commerce Clause: An Historical Prospective," 29 Vand. L. Rev. 335 at 347-348 stated:

> "Conflicting methods of division of income or other tax bases that result in taxation of more than one hundred percent of the base are inequitable and oppressive to multistate taxpayers. Diversity in state or local tax apportionment, which often results in overall undertaxation of an enterprise, is likewise unfair to the governments and oppressive to competitive intrastate businesses. Nevertheless, the Supreme Court consistently had taken the position, long before 1959, that it is beyond its constitutional province to prescribe methods of dividing income or other tax bases for the states, and that diverse and conflicting methods of apportionment, mischievous though they be, do not violate the commerce clause or the due process clause, so long as each state's method, considered on its own merits, is not repugnant to the Constitution. In my judgment, the Court is on solid constitutional ground and is eminently wise in holding to this position. Unless adequate collaborative action is taken by the states—perhaps along the lines of the Multistate Tax Compact—to achieve substantial uniformity in the division of the net income and other measures, this is an area that calls for congressional regulation. The courts cannot do the job; only the states and Congress are equipped to develop and administer workable policies."

We thus respectfully disagree with the position of Mobil and its amicus in this case that fiscal policy considerations support their claimed tax immunity based on the application of the legal fiction of commercial domicile. We believe that Mobil's income from its intangible properties derived from and utilized in its integrated unitary business should be distributed "wherever * * * its work is done" (*Adams Express Co. v. Ohio State Auditor, supra* at 166 U.S. 223).



### 3. The History and the Judicial Decisions do not Support Taxation of Dividends Only by the State of Commercial Domicile, But Rather, Support the Inclusion of Dividends in Apportionable Income for State Income Attribution Purposes if the Stocks and the Income Derived Therefrom are Acquired and Managed as an Integral Part of the Taxpayer's Unitary Business which it Conducted in Part in the Taxing State.

As heretofore indicated on pages 45-47 of this brief, this court has traditionally upheld the inclusion of the entire net income of a multistate/multinational corporation in apportionable net income so long as the taxpayer has not established, by clear and cogent evidence (1) that the apportionment result taxes income not reasonably related to instate activities or sources; or (2) that the income included in apportionable income is unrelated to or disassociated from the business carried on in part in the taxing state.

Nevertheless, on pages 29-30 of its brief, Mobil asserts that history and judicial decisions support the "taxation of dividends" *only* by the state of commercial domicile.

In regard to Mobil's "history" aspect of this argument, we fail to see its relevancy if there otherwise existed any such "history." While Mobil cited Volume 1 of the "Willis Report" (Ibid., footnote 34) at page 204 et seq. in support of its history argument, an examination of the analysis contained therein reveals no such history. As to those states which employ "specific allocation" of dividends and other forms of intangible property, the Willis Report concluded:

> "Because of the difference in the types of income subject to allocation and the variety in attribution rules, the treatment given to a particular item may vary substantially. With regard to such income as interest, dividends, rents and royalties, and capital gains there are no rules of universal applicability. Instead, so diverse is the treatment that the diversity

itself lends support to the conclusion that it is futile to search even in theory for the single true source of any particular item of income earned by a multistate taxpayer.

Specific allocation creates more than mere theoretical problems. Since taxpayers are required to calculate their liabilities in exact dollar amounts, rules for allocating particular types of receipts can create complex compliance problems." (Willis Report, *Ibid.*, footnote 34 pp 216-217)

Based on these considerations, the Willis Report recommended apportionment of all income, without the use of either "separate accounting" or specific allocation.[39]

Furthermore, to the extent that "history" is relevant, we believe current "history" is more significant. Mobil admits and Appendix F of its brief (pages 37a-39a) indicates that the vast majority of the states now apportion taxable dividend income.[40]

Twenty-nine states apply the unitary concept in accordance with UDITPA standards.[41]

Thus, to the extent that dividends constitute "business income" (which is presumptively the nature of Mobil's dividends in question since there is no showing that its stocks in question and the income derived

[39]Report of the special Subcommittee on State Taxations of Interstate Commerce of the Committee on the Judiciary House of Representatives, Volume 4, Part VI—Recommendations (H. Report No. 952, 89th Cong. 1st Sess., September 2, 1965) pages 1135 and 1144.

[40]As indicated *supra* at pages 72-75, there is apparently no state that would tax dividends based solely on the legal fiction of "commercial domicile" under the facts and circumstances of this case. The states generally apply the unitary concept to determine what constitutes apportionable income.

[41]UDITPA apportions dividends and all other income to the extent that constitute business income in accordance with the definition of business income contained in Section 1(a) of UDITPA which reads:

"Business income" means income arising from transaction and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.



therefrom, were not acquired and used by Mobil in its integrated business operations subject to apportionment in part in Vermont), "history" refutes, rather than supports, the historical argument of Mobil.

In regard to judicial precedent, the case relied upon by Mobil in footnotes 16 and 17 of its brief (pages 29-30) do not support its argument.

These cases do not support the proposition that dividends are taxable by any state for income tax purposes by mechanical application of the legal fiction "commercial domicile." In fact, judicial precedent establishes the apportionment of dividends if the stocks and dividends constitute a part of the unitary business carried on in the state. This is simply a modern application of the "business situs" rule which in turn is the substance of the "commercial domicile" rule.

The cases have universally held that the income of a unitary business which is connected with business activities carried on in part within a taxing state may be subject to formulary apportionment even though derived from intangible properties. In *International Harvester v. Department of Taxation*, 322 U.S. 435 (1944), and *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435 (1940), this Court upheld the apportionment of income from dividends against the payor corporation based on its instate activities. In *Montgomery Ward & Co. v. Commissioner of Taxation*, 276 Minn. 479, 151 N.W.2d 294 (1967), and *Great Lakes Pipeline Co. v. Commissioner of Taxation*, 272 Minn. 403, 138 N.W.2d 612 (1965), app. dism'd 384 U.S. 718 (1966), the Court held that interest income was business income subject to apportionment.

In *F. W. Woolworth Co. v. Director of Division of Taxation*, 45 N.J. 466, 213 A.2d 1 (1965); *Gulf Oil Corp. v. Morrison*, 120 Vt. 324, 141 A.2d 671 (1958); and *F. W. Woolworth Co. v. Commissioner of Taxes*, 130 Vt. 544, 298 A.2d 839 (1972), the Courts held that dividend income was subject to apportionment either as business income or as a part of the unitary income of the payee corporation. In

*Sperry & Hutchinson Co. v. Department of Revenue*, 270 Or. 329, 527 P.2d 729 (1974), the Court held that interest income used in the trade or business of the taxpayer was subject to apportionment under UDITPA. As indicated in *Appeal of W. J. Voit Rubber Co., May, 1947 C.C.H. Cal. Tax Rep. para. 202-435*, and cases cited therein, the California Board of Equalization has always held that income from a unitary business, whether from intangible properties or otherwise, is subject to formulary apportionment. In *In Re Goodyear Tire & Rubber Co. Corporate Income Tax 1966, 1967, 1968*, 133 Vt. 132, 335 A.2d 310 (1975), the Court upheld the apportionment of dividend income.[42]

The income apportionment decisions of this court have likewise sustained the apportionment of the entire income of a unitary trade or business. None has ever upheld a hybrid combination of "separate accounting" and apportionment of unitary income—the method Mobil and its amicus curiae here urge should constitute the due process and commerce clause constitutional standard.

### 4. Decisions of this Court Do Not Support Exclusion of So-Called "Foreign Source" Dividends from Apportionable Income for Income Attribution Purposes.

Mobil's argument that decisions of this Court support its exclusive "commercial domicile" jurisdictional argument (App. Br., pp. 34-36) is refuted by all of the unitary apportionment decisions of this Court from *Adams Express, supra*, through *Moorman, supra*.

[42]See the cases discussed at pages 40-47, *supra*, and the following: *Maxwell v. Kent-Coffey Mfg. Co., supra*, 204 N.C. 355, 168 S.E. 379 (1933), aff'd 291 U.S. 642 (1934); *Cleveland Cliffs Iron Co. v. Corp. & Sec. Com.*, 351 Mich. 652, 88 N.W.2d 564 (1968); *ASARCO v. Montana Dept. of Revenue*, 567 P.2d 901 (Mont. 1977); *Champion International Corp. v. Bureau of Revenue*, 88 N.M. 411, 54 P.2d 1300 (1975); *Qualls v. Montgomery Ward*, Sup. Ct. of Ark., dec'd July 2, 1979; *Albany International Corp. v. Halperin*, 388 A.2d 902 (Me. 1978); *Johns-Manville Products Corp. v. Comr. of Rev. Admin.*, 115 N.H. 428, 343 A.2d 221 (1975).



Mr. Justice Rutledge's concurring and dissenting opinion in the sales and use tax cases of *McLeod v. Dilworth Co., supra; General Trading Co. v. State Tax Commission, supra;* and *International Harvester Co. v. Evatt, supra*, at 322 U.S. 349 (considered *supra* at page 61 in connection with Mobil's "risk" argument) is totally irrelevant. There is a vast difference between income tax attribution rules as applied to the unitary income of a multinational business and sales or use tax attribution rules applied to interstate sales transactions. This is demonstrated by the specific facts of *Moorman*. If Mobil's sales and use tax jurisdiction analogy is controlling, this Court could have disposed of *Moorman* by simply holding that Iowa had exclusive jurisdiction to tax the entire net income of any interstate sales with Iowa destinations, even though some income therefrom was shown to be specifically attributable to out-state activities and sources. This it did not do.

## G. The Inclusion of "Federal Taxable Income" In Apportionable Income for Vermont Income Tax Purposes Does Not Conflict with Any Federal Policy in Regulating Foreign Commerce Because it Does Not Constitute the Regulation of or Taxation of Foreign Commerce and Because There Otherwise Exists No Federal Policy with Which it is in Conflict.

On pages 38-48 of its brief, Mobil argues that the Vermont tax should be invalidated by this Court "on the ground that it conflicts with established federal policy in regulating foreign commerce." (App. Br., p. 38) Mobil assumes that the income taxed by Vermont is from "that foreign commerce conducted by United States based enterprises." (App. Br., p. 39)

Mobil and its amicus, in arguing this proposition, fail to address their argument to the initial question of how the inclusion of dividends of a domestic United States Corporation, in apportionable income, constitutes either a

regulation of foreign commerce or a tax on foreign commerce under the Constitution. Vermont is not imposing any tax on either "foreign commerce" or any income which Mobil derives from "foreign commerce." To the extent that Mobil engages in any foreign commerce, the Vermont apportionment formula attributes this alliquot part of Mobil's income to foreign commerce.

Assuming arguendo that Vermont's inclusion of dividend income in apportionable income could be construed to constitute taxation of income from foreign commerce, still Mobil has established no basis for its conclusion that this is unconstitutional inference, in any manner, with foreign commerce or international relations of the federal government. Vermont is not including in its income tax base any income which is not included in federal taxable income and in fact taxed by the United States.

It is immaterial that the Internal Revenue Code, solely for United States income tax purposes, allows a partial tax credit for foreign taxes on certain dividend income under different jurisdictional and complex income tax attribution rules solely for federal income tax purposes. This is particularly true (1) when such credits do not eliminate any effective taxation by the United States of the dividend income of domestic United States corporations; and (2) when there is no showing here how these credits apply to Mobil's dividends in question. While partial double taxation of dividend income is eliminated at the federal level under the Internal Revenue Code by the partial tax credit device, at the state level it is assured by the application of apportionment rules.

Nor does the special dividend deduction provided for in the I.R.C., Sec. 243 support Mobil's argument. It pertains only to *double taxation by the United States of the dividends of domestic corporations at the corporate level irrespective of "source."* This deduction has nothing to do with the issue of double taxation of foreign source dividend income. Vermont allows this deduction automat-



ically by including only "federal taxable income" in apportionable income. Also, Vermont has not subject to taxation any of the profits of Mobil's subsidiary and affiliated corporations. Thus, any analogy to § 243 is misplaced.

Neither does the network of treaties between the United States and foreign countries have anything to do with the question at issue. These treaties are entered into by the United States to protect their own citizens, residents and domestic corporations from inappropriate or discriminatory taxation *by other nations.* They do not restrict how the United States chooses to tax its own citizens, residents or domestic corporations. Any such United States tax policy can be fully implemented without any treaty. It is solely a matter of concern of the states and the Congress. To the extent these treaties have anything to do with state taxation, they expressly so provide.

The fallacy of the foreign policy argument of Mobil and its amicus is demonstrated by the conclusions of the Willis Committee that a state income tax base should conform to international tax policy of the United States, and that it does conform to this policy if a state income tax base includes only federal taxable income. As stated in the recommendations of the Willis Committee:

> "* * * if a corporation is considered to have income from sources outside the United States and that income is taxable by the United States, such income could be included in a state's tax base prior to apportionment and the state would not be required to include property or payroll located outside the United States in its apportionment formula. *These rules would apply to corporations incorporated in the United States and are designed to make available for apportionment among the states all of the tax base available to the United States.*" (Emphasis added, Report of the Special Subcommittee on State Taxation of Interstate Commerce, H.R. No. 952 89th Congs., 1965, Vol 4, p. 1155)

Neither do the cases of *McGoldrick v. Gulf Oil Corp.*, 309 U.S. 414 (1940) or *Japan Line, supra,* support the

"foreign policy" argument of Mobil and its amicus. The *McGoldrick* case involved the application of a specific tax immunity policy incorporated in a specific federal statute.

The *Japan Line* decision was based on a very definite federal statutory and regulatory pattern as well as a clearly defined international tax policy among the nations of the world which were designed to exempt instrumentalities of international commerce from any property taxation except by the domicillary nation.

In the instant case there is absolutely no federal or international policy which in any way supports the argument that dividend income of domestic United States payee corporations, irrespective of the country of incorporation or location of the business activities of the payor corporation, shoud be taxed only by the state of the "commercial domicile."

## CONCLUSION

Mobil and its amicus ask this Court to invalidate Vermont's corporate income tax statute, as applied to Mobil, under the facts and circumstances of this case. In so doing, they advance various abstract and hypothetical arguments, which on close analysis, are devoid of any constitutional significance. Their due process argument is frivolous since it is based on the twin invalid assumptions (1) that Vermont has imposed a tax on its dividend income which it derives from activities without Vermont; and (2) that income from out-of-state activities cannot be included in apportionable net income. These assumptions ignore the nature of a net income tax and the significance of reasonable apportionment rules.

Their commerce clause argument, in addition, is based on the assumption that reasonable apportionment rules are invalid if they expose any item of income included in apportionable income to a speculative risk of multiple taxation. They further assume that this Court's function under the commerce clause is to mandate uniform national rules to avoid any such speculative risk



as pertains to what they label as "foreign source income." In support of this argument, they rely on *Japan Line* and purport to distinguish *Moorman* and other apportionment decisions of this Court. Since *Japan Line* is clearly distinguishable and *Moorman* and other unitary apportionment decisions of this Court are directly in point, the "foreign commerce" argument of Mobil and its amicus likewise lacks any merit.

It is therefore respectfully submitted that this Court should affirm the Vermont Supreme Court decision and find that the Vermont apportionment formula, as applied to Mobil's federal taxable income, is valid in every respect inasmuch as Mobil has not established that Vermont has taxed any net income of Mobil not reasonably related to its Vermont business for the years in question.

DATED this 14th day of August, 1979.

Respectfully submitted,

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